THE APPLICATION OF CORPORATE GOVERNANCE IN LARGE AND MEDIUM-SIZED SOUTH AFRICAN AUDITING FIRMS

by

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THESIS

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DECLARATION

I certify that the thesis submitted by me for the degree Doctor of Philosophy in Auditing at the University of Johannesburg is my independent work and has not been submitted by me for a degree at another university.

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ABSTRACT

This study examines the corporate governance of large and medium-sized auditing firms in South Africa. Auditing firms serve the public interest; it is therefore important for these firms to disclose relevant corporate governance information to the public and to practice good corporate governance principles. Due to a string of corporate scandals in recent years, the audit profession has been criticised and has come under media scrutiny. This has undermined the reputation of the profession, with experts and the public questioning whether auditing firms have corporate governance structures in place, and whether they are taking public interest into consideration.

This study contributes to the existing body of academic knowledge by pursuing the following six objectives: (1) examining the development of corporate governance in the UK, USA, Australia, the Netherlands, and more specifically, in South Africa; (2) conducting a comparison between the UK Audit Firm Governance Code and King IV to identify the similarities; (3) exploring how the lack of corporate governance has contributed to some of the worst financial corporate failures in the UK, USA, Australia, the Netherlands and South Africa to establish whether auditing firms contributed to these failures; (4) determining the current legal and governance structures in auditing firms as well as the challenges associated with implementing corporate governance principles within auditing firms; (5) identifying what corporate governance practices are disclosed by firms; (6) determining the current corporate governance practices in auditing firms; and obtaining the expert opinions of the CEOs of auditing firms about corporate governance in auditing firms.

To achieve these objectives, a pragmatist paradigm was applied. Both qualitative and quantitative information was gathered for analysis. The data was independently analysed and the qualitative results were then converted into quantitative data that was correlated with the quantitative results. A data transformation triangulation design was applied in this study. The secondary data was obtained from publicly accessible information published on the websites of the auditing firms. It included the firms' transparency reports and integrated reports. Content analysis was selected to collect the qualitative data. The primary data was obtained through questionnaires which were self-administered. The results revealed that the auditing firms are not disclosing or applying corporate governance principles and practices to the necessary extent. The CEOs of the auditing firms did, however, indicate that the principles and practices contained in the UK Audit Firm Governance Code were important and should be applied by auditing firms in South Africa. This finding confirmed that a corporate governance code for South African auditing firms should be developed in the future.

The findings of the analysis corroborated those found in the literature, thus confirming the stated objectives. From these analyses, best practice recommendations were formulated as well as regulatory and statutory recommendations. Among these best practice recommendations were that auditing firms start implementing the relevant principles of King IV until further developments in future. It is also recommended that auditing firms appoint oversight boards which consist of members who are independent. Auditing firms should also consider combining their transparency reports and integrated reports as it would minimise the duplication of information.

The statutory and regulatory recommendations included that the IoDSA consider the inclusion of a sector supplement for auditing firms in future King Code iterations. The IRBA should consider providing guidelines to auditing firms on corporate governance practice and disclosure. Amendments to the APA should be considered to facilitate the appointment of INEDs for auditing firms.

Keywords: Corporate governance, auditing firms, independence, stakeholders, public interest, EXCO, oversight board, transparency report, integrated report.

STUDY CUT-OFF

CUT OFF DATE

The cut-off date for this study is 31 August 2020. Any developments after this date will be taken into consideration in future studies.

DEDICATION

I dedicate this thesis to my mother, Marietjie Grobbelaar, for her continuous support and for the inspiration and role model that she is to me. She taught me how to be the strong, courageous and hard-working woman that I am today, and for that I will forever be grateful.

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LIST OF ABBREVIATIONS

ABN	Algemene Bank Nederland
AGM	Annual General Meeting
AICPA	America Institute of Certified Public Accountants
AIG	American International Group
AMRO	Amsterdamsche en Rotterdamsche Bank
ANZ BANK	Australia and New Zealand Banking Group
APA	Audit Profession Act
ASIC	Australian Securities and Investment Commission
ASX	Australian Stock Exchange
BCCI	Bank of Credit and Commerce International
BDO	Binder Dijker Otte
BHS	British Home Stores
CA (SA)	Chartered Accountant (South Africa)
CACG	Commonwealth Association for Corporate Governance
CCC	Commercial Companies Code of 2000
CDO	Collateral Debt Obligations
CEO	Chief Executive officer
CFO	Chief Financial Officer

CGC	Corporate Governance Code
CIPC	Companies and Intellectual Property Commission
CLERP	Corporate Law Economic Reform Program
CMA	Capital Markets Authority
CO	Code of Obligations
CPA	Certified Professional Accountant
CSR	Corporate Social Responsibility
Deloitte	Deloitte and Touche
ECGI	European Corporate Governance Institute
ED	Exposure Draft
EU	European Union
EXCO	Executive Committee
EY	Ernst & Young
F&H	Friehling & Horowitz
FBI	Federal Bureau of Investigation
FRC	Financial Reporting Council
GAAP	Generally Accepted Audit Principles
GE	General Electric
GEPF	Government Employee Pension Fund
IAASB	International Auditing and Assurance Standards Board

ICAEW	Institute of Chartered Accountants in England and Wales
ICSA	Institute of Chartered Secretaries and Administrators
Inc.	Incorporated
INED	Independent Non-executive Director
ING	International Nederlanden Group
IoDSA	Institute of Directors in Southern Africa
IOSCO	International Organisation of Securities Commissions
IRBA	Independent Regulatory Board for Auditors
ISA	International Standards on Auditing
ISQC 1	International Standard on Quality Control
ISQM 1	International Standard on Quality Management
IT	Information Technology
ITC	Invitation to Comment
JSE	Johannesburg Stock Exchange
King I	King I Report on Corporate Governance
King II	King II Report on Corporate Governance
King III	King III Report on Corporate Governance
King IV	King IV Report on Corporate Governance
KPI	Key Performance Indicator
LSE	London Stock Exchange

MBS	Mortgage Backed Securities
MCC	Maxwell Communications Corporations
MGN	Mirror Group Newspapers
MP	Member of Parliament
Nasdaq	National Association of Securities Dealers Automated Quotations
NCCG	Norwegian Code of Practice for Corporate Governance
NYSE	New York Stock Exchange
OECD	Organisation for Economic Co-operation and Development
PCAOB	Public Company Accounting Oversight Board
PIE	Public Interest Entities
PwC	PricewaterhouseCoopers
SAAPTI	South African Auditing Profession Trust Initiative
SACOB	South African Chamber of Business
SAICA	South African Institute of Chartered Accountants
SEC	Securities and Exchange Commission
SENS	Stock Exchange News Service
SFO	Serious Fraud Office
SOX	Sarbanes Oxley Act
SPE	Special Purpose Entity
SPSS	Statistical Package for the Social Sciences

UK	United Kingdom
URL	Uniform Resource Locator
USA	United States of America
VBS	VBS Mutual Bank

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Chapter 1: INTRODUCTION AND STUDY OVERVIEW

1.1 Introduction

The recent spate of corporate failures[1] across the globe, such as Enron and WorldCom (Segal, 2018), has attracted attention from corporate regulators and professional bodies. In South Africa, the Eskom and Tongaat scandals of 2019/2020 were preceded by the Steinhoff and VBS Bank corporate failures of 2017/2018, and before that, LeisureNet, Regal Treasury Bank and Randgold & Exploration, to name a few. Although corporate failures are not new, it is of increasing concern to stakeholders that many of these unexpected failures were of apparently financially robust companies. One of the repercussions of these failures has been the reputational damage of auditing firms as well as aspersions cast upon the audit process and the accounting profession in general (Kilgore, 2007).

There are several examples of corporate failures leading to audit firm failures[2], such as the case of Enron, where their auditors, Arthur Anderson, subsequently collapsed as well (Crotty, 2019). In South Africa, the auditing firm, KPMG, made headlines for their involvement in the Gupta and VBS Bank Scandals (Pilling, 2017), which led to changes in their leadership, changes to the governance structure of KPMG South Africa and improved quality control procedures in specific areas within the entity (Cotterill, 2017). This had a serious effect on the reputation of the auditing firms, and the profession as a whole.

These real or alleged corporate scandals[3] and audit failures[4] have had material consequences by undermining public confidence in corporate governance and accountability. These corporate scandals and audit failures raise the familiar cry of ‘Where were the auditors?’. Such crises are often managed by state and professional bodies, which promise reforms, revising auditing or accounting standards, tweaking regulatory structures, disciplining accountants and auditing firms and promoting ethical guidelines. Domestic and international auditing standards are also relatively

[1] Corporate failure is defined in section 1.3.
[2] Audit firm failure is defined in section 1.4.
[3] Corporate scandal is defined in section 1.3.
[4] Audit failure is defined in section 1.3

silent on the social obligation of auditing firms, with the exception of some codes such as the International Standard on Quality Control (ISQC). Strategies for managing crises at auditing firms pay very little attention to the values and governance processes that direct auditing firms. Therefore, audit failures continue unabated (Sikka, 2003).

According to Sikka (2003), audit failures are often the result of the values that govern auditing firms. This view is supported by Peiter Koornhof of Allan Gray (an investment management company in South Africa), who states that major crises usually reflect a governance breakdown at multiple layers (Crotty, 2019). Sikka (2003) suggests that any reform of auditing and accountancy should bring about a major change in the values that govern auditing firms. He further states that the success of an auditing firm is measured by profits, rather than the service provided to all stakeholders. He states that auditing firms are entrepreneurial and find new ways of selling their services to the public. According to the Financial Reporting Council (FRC) of the United Kingdom (UK) (2010), strong audit firm governance is a way in which auditing firms can maintain public trust (Amirul, Salleh & Abu Bakar, 2015). Unfortunately, at present, the corporate structures of some auditing firms seem to be flawed as they do not apply codes of corporate governance (Aberian, 2019). Currently in South Africa, there is no corporate governance structure that regulates the corporate governance of auditing firms. From the literature, it is evident that the UK is at the forefront of corporate governance within auditing firms. No evidence of other corporate governance codes, specifically with reference to auditing firms, could be found.

For this reason, this study aims to determine whether corporate governance guidelines could be provided for South African auditing firms to ensure that they too, adhere to sound corporate governance principles and practices. The next section discusses the developments in corporate governance.

1.2 Evolution of corporate governance

1.2.1 Corporate governance background

In the 1970s the term ‘corporate governance’ came into use (Pargendler, 2016). It is often used to describe the principles or rules that govern relationships between corporate participants in publicly-traded firms. The term especially refers to the relationships between directors, shareholders, managers, and sometimes employees (Aziri, 2014).

Corporate governance was formally defined in 1992, in the UK, with the release of the Cadbury Report on Corporate Governance. Before the Cadbury Report, corporate governance was simply a topic that was discussed and debated by many (Marx, 2008). The Cadbury Committee defined corporate governance as "*the system by which companies are directed and controlled*" (Committee on the Financial Aspects of Corporate Governance, 1992:18). Over the years many other definitions were released, but according to Marx (2008), corporate governance is, in essence, the system by which entities are controlled and directed.

Other contributors to corporate governance literature expand the definition to the following:

> …a set of responsibilities and practices exercised by the board and executive management with the goal of providing strategic direction, ensuring that objectives are achieved, ascertaining that risks are managed appropriately and verifying that the enterprise's resources are used responsibly (ITGI 2003:6).

> The exercise of ethical and effective leadership by the governing body towards the achievement of the following governance outcomes: ethical culture, good performance, effective control and legitimacy (IoDSA, 2016:11).

Besides the obvious differences between the definitions cited above, most address an element of the entity's responsibility towards various parties. This could include the responsibility of the corporation towards the shareholders, the stakeholders and the general public (Aziri, 2014).

Based on the discussion above, the following definition of corporate governance has been formulated for the purposes of this study:

> *A set of responsibilities and practices instituted by the governing body in order to direct a company to achieve its strategic objectives while remaining sustainable, accountable and transparent, and acting in the best interest of all the stakeholders.*

Historically, corporate governance only focused on the relationship between governing bodies, shareholders and management. Its main objective was to address agency conflicts and ensure that the agents employed by business owners managed the organisation in a way that served the best interests of the shareholders (Panda & Leepsa, 2017). However, as a result of increased stakeholder interests and regulatory developments, the concept of corporate governance has evolved to become more inclusive in nature, taking into account the rights of all stakeholders involved in the corporate wealth creation process. Corporate governance further addresses issues relating to ethics, accountability, transparency and disclosure as well as organisations' social and environmental impact (Raemaekers, 2014; Institute of Directors in Southern Africa [IoDSA], 2009).

The Organisation for Economic Co-operation and Development (OECD) (2015a) states that effective corporate governance is meant to guide those charged with governance in their decision-making processes to create sustainable, long-term value through market confidence and business integrity. It forces companies to actively engage with the society in which they exist, and not only consider financial prosperity but to also take into account social and environmental value creation (Raemaekers, 2014). Kakabadse and Korac-Kakabadse (2002) agree, stating that corporate governance requires processes and procedures that serve as guidelines for accepted behaviour for both companies and society. Corporate governance should therefore be of a diverse nature that is inclusive in its decision-making and should support the weaker elements of society in pursuit of the common good (Frederikson, 1992).

Humans display characteristics of self-interest and opportunism and therefore there is a need for corporate governance to ensure that those who are in a position of trust, act in the best interests of all stakeholders (Maseko, 2015). Barrier (2003) reiterates this statement, contending that organisations are expected to operate as good corporate citizens because they have an influence on the lives of many individuals.

In simple terms, corporate governance is characterised by ethical and effective leadership. It requires those charged with governance to exemplify ethical leadership in discharging their responsibilities by demonstrating high levels of integrity, objectivity, competence, responsibility, accountability, fairness and transparency. At the same time, however, corporate governance requires those charged with governance to lead their companies towards the achievement of strategic objectives (IoDSA, 2016).

It is widely recognised that corporate governance can contribute to the long-term sustainability and the economic success of corporations (Armstrong, 2003, as quoted by Rossouw, 2005). Rossouw (2005) agrees, stating that corporate governance can improve the reputation of companies and enhance corporate responsibility, which attracts foreign and local investors. Maseko (2015) adds that the boundaries of accepted behaviour for societies and organisations are set by effective leadership and corporate governance.

After the release of the Cadbury Report in 1992, many other countries developed their own corporate governance codes. The next section briefly explores the corporate governance developments that took place in various countries around the world. Chapter 2 contains a more detailed discussion of corporate governance and international developments—the literature review on corporate governance.

1.2.2 Corporate governance developments globally

Corporate collapses and business failures, combined with fraudulent financial reporting practices, created a need for corporate governance developments. This combination of factors gave rise to various corporate governance codes that were issued across the world since 1992 (Marx, 2008). This study focuses on the UK, the United States of America (USA), Australia, the Netherlands and South Africa, for the reasons provided below.

The USA corporate governance practices are respected because the country was the first across the globe to legislate some key aspects of corporate governance compliance, culminating in the enactment of the Sarbanes Oxley Act (SOX) in 2002 (Langeni, 2018).

The UK was selected due to its long history with corporate structures as well as governance in general. As mentioned earlier, the first formal code on governance was the UK-authored Cadbury Report of 1992 (Langeni, 2018). The UK is also the only country with a corporate governance code specifically for auditing firms, namely, the Audit Firm Governance Code (FRC, 2010).

According to a survey conducted by KPMG in 2015, Australia ranked equal fourth for its corporate governance regime, only outranked by the UK, the USA and Singapore. This is particularly interesting given that Australia does not have the regulatory overlay present in the UK or the USA.

There is a significant commitment in Australia to reducing red tape around corporate governance and using a strong principles-based approach, which appears to be working well (KPMG, 2015).

The Netherlands is one of a handful of countries to apply a two-tier board structure model, which is also different to the countries mentioned above. The two-tier board structure is a requirement of the Dutch Corporate Governance Code, which is applicable to all listed entities. From the integrated reports of the auditing firms in the Netherlands, these firms have also adopted this principle. For this reason, the Netherlands was selected as one of the countries for the literature review (Bendixen & Thomas, 2000).

South Africa was selected for this study, as there have been various corporate failures in the country, which have resulted in audit failures. It was only after the Gupta and VBS corporate failures that KPMG decided to implement principles of the King IV Report on Corporate Governance (King IV) in their organisation. This raised the question, 'Why had auditing firms not applied King IV prior to these corporate failures?' One of the reasons could be that there is currently no sector supplement in King IV for auditing firms. There are specific sector supplements for municipalities, non-profit organisations, retirement funds, small and medium enterprises and state-owned entities. These sector supplements are primarily aimed at the governing body of these entities, as this is the focal point of corporate governance within the organisations (IoDSA, 2016). Unfortunately, as stated earlier, there is no sector supplement for auditing firms. It also within this context that the research gap was identified and the research question formulated.

Below is an explanation of the corporate governance developments in the countries mentioned above.

1.2.2.1 Corporate governance developments in the UK

In the late 1980s, there was a string of sensational business scandals in the UK. The scandal of Robert Maxwell, in which pension funds were plundered, created outrage in the public. This too was the case with the Bank of Credit and Commerce International, where the auditors failed to expose the bankruptcy and the high pay rises of the senior business executives. Consequently, a special committee was formed by the City of London to examine the financial aspects of corporate governance. This resulted in the Code of Best Practice produced by the Cadbury Committee. Sir

Adrian Cadbury, an industrialist, chaired this committee. This report, which became known as the Report of the Cadbury Committee, consisted of guidelines through which the activities of company directors and executives could be controlled to ensure ethical conduct. The Cadbury Report (1992) defined corporate governance as the systems by which companies are directed and controlled. The Report suggested that non-executive directors should play a bigger role on corporate boards and that board operations should involve a more active role for auditors (Boyd, 1996). In 1995, the Cadbury Report was reviewed, giving rise to the Myners Report (Pandhu, n.d.).

In July 1995, another review was done, and the Greenbury Report was published, suggesting more principles for inclusion into the new Report. It was suggested that the board of directors should appoint a remuneration committee, which should consist of non-executive directors. It was also suggested that directors should have long-term, performance-related pay, which should be disclosed in the annual reports of the company, and that the directors' contracts should be renewable each year. The Report also suggested that progress should be reviewed every three years. In 1998, Sir Ronald Hampel, who was chairman and managing director of Imperial Chemical Industries plc, chaired a third committee. This committee drafted the new report, namely the Hampel Report, which was issued in 1998 (FRC, n.d.).

Next in 2010 followed the Combined Code, which was a consolidation of all the principles in the Cadbury, Myners, Greenbury and Hampel Reports. The Combined Report included principles stating that the chairman of the board should be seen as the 'leader' of the non-executive directors. It also suggested that institutional investors should consider voting the shares they held at meetings, though it rejected compulsory voting and the disclosure of all kinds of remuneration, including pensions.

In 2010, a new version of the UK Corporate Governance Code was submitted (FRC, n.d.).

This Code (formerly the Combined Code on Corporate Governance) promotes corporate governance, with an emphasis on the relationships between stakeholders, shareholders and organisations. It also emphasises that the corporate culture of an organisation should be aligned with the company's values, business strategy and purpose and that it should promote diversity and integrity. The Code provides guidance on how organisations should apply its provisions.

Companies are also required to disclose how they complied with the provisions, or provide an explanation if they were unable to comply (FRC, n.d.).

In 2010, the FRC introduced the Audit Firm Governance Code. This Code was drafted to serve the interests of shareholders of listed companies to whom auditors address their reports. The objective of this Code was to ensure that auditing firms were seen as a good example of best practice governance, to enrich the transparency of auditing firm reports and to encourage changes in the governance of auditing firms. It also aimed to ultimately improve the way in which auditing firms are managed and to strengthen the regulatory regime by achieving effective and transparent governance without disproportionate regulation. It was recommended that auditing firms which audit public interest entities should comply with the provisions of the Code or give a considered explanation in cases where they cannot comply (Institute of Chartered Accountants in England and Wales [ICAEW], 2010). From all the literature reviewed, it can be seen that the UK is the only country that has a corporate governance code specifically for auditing firms.

1.2.2.2 Corporate governance developments in the USA

The expression 'corporate governance' did not even exist in the English language until the 1970s (Pargendler, 2016). In the mid-1970s, the federal Securities and Exchange Commission (SEC) brought corporate governance on to the official reform agenda. Thus, the term 'corporate governance' first appeared in the Federal Register in 1976 (Cheffins, 2012).

In the 1990s, as the USA economy recovered from the recession, the Anglo-Saxon model of corporate governance turned into a blueprint for financial and economic development around the world (Pargendler, 2016). The enactment of the SOX Act of 2002 was one of the most significant changes that occurred in the USA. It included a statutory requirement for audit committees and various corporate governance changes (Marx, 2008). The introduction of the SOX in 2002 was widely regarded as the most extensive USA federal law related to corporate governance (Uzun, Szewczyk & Varma, 2004). SOX was enacted to restore confidence in the markets after several high-profile corporate governance scandals in the USA (Cheffins, 2010).

Another important response to the corporate scandals was that companies which traded on the New York Stock Exchange (NYSE) or listed on National Association of Securities Dealers Automated

Quotations (Nasdaq) had to comply with various corporate governance provisions. The SOX of 2002 and the NYSE and Nasdaq proposals imposed several corporate governance provisions on publicly traded companies in the USA, with significant emphasis on improved oversight by the companies' independent directors (Uzun et al., 2004).

1.2.2.3 Corporate governance developments in Australia

In Australia, Professor Ramsay—a Harold Ford Professor of Commercial Law at the Melbourne Law School and Director of the Centre for Corporate Law and Securities Regulation—produced a report in October 2001 detailing issues concerning the auditing profession as well as the current requirements on the independence of company auditors (Mirshekary, Yaftian & Cross, 2005). Following the Ramsay Report, in September 2002, a Discussion Paper named *Corporate disclosure – Strengthening the financial reporting framework* was released as part of the Corporate Law Economic Reform Program (CLERP 9) (Marx, 2008).

In April 2003, Justice Neville Owen submitted the Report of the HIH Royal Commission into the collapse of HIH Insurance Group Ltd. The CLERP 9 bill, which was tabled in Parliament in December 2003 and came into force in July 2004, was influenced by these three documents. In August 2002, a Corporate Governance Code was introduced by the Australian Stock Exchange (ASX) while in March 2003, the first edition of the Corporate Governance Code's Principles of Corporate Governance and Best Practice Recommendations was released. These ten principles were only guidelines, and not prescriptive. If listed companies chose not to adopt a certain principle, they had to provide an appropriate reason as to why they had not done so (Hay & Redmayne, 2017).

In 2007, after an extensive review, a second edition was released. This edition contained only eight principles and the title of the document was shortened to Corporate Governance Principles and Recommendations. In 2010, additional amendments were made to the second edition. Another review was conducted in 2012–2013 to ensure that international trends in corporate governance were applied. This review resulted in the release of a third edition in March 2014. According to Hay and Redmayne (2017), the structure of the eight principles was simplified and there was more flexibility with regards to the disclosure requirements.

In 2017, after several emerging issues regarding values, trust and culture in listed entities, the ASX Corporate Governance Council decided to develop the fourth edition of the Principles and Recommendations. This new edition, which became applicable on 1 January 2020, consisted of eight principles that needed to be complied with by all listed entities (ASX Corporate Governance Council, 2019).

1.2.2.4 Corporate governance developments in the Netherlands

In 2004 the first Dutch Corporate Governance Code came into effect. This Code was applicable to all listed entities. In December 2016, a revised version of the Code was published, focusing more on culture, risk management, the reporting of misconduct and long-term value creation. It also addressed how the principles of the Code should be applied in a company with a one-tier board. A comply or explain system was adopted for the Code. According to the Code, companies had to disclose on their websites how they had applied the Code's principles and best-practice provisions. In the case where they were unable to do so, an explanation had to be provided. There is a separate monitoring committee that annually reports on the extent to which the Code is complied with and any problem areas that are identified (European Corporate Governance Institute [ECGI], 2020).

1.2.2.5 Corporate governance developments in South Africa

The notion of corporate governance and the development of related guidelines and codes has been a prominent feature in South Africa's business environment since the early 1990s (Marx, 2008). The reasons for this are indicated by various researchers as follows:

- The need to restore confidence and trust in South African institutions following the apartheid era (Burke & Clark, 2016);
- The need for robust market discipline and corporate reform in order to attract and retain foreign investors (Marx, 2008; Maseko, 2015);
- The expectation for South African companies to play a role in addressing the socio-economic challenges facing the country (Croucher & Miles, 2010);
- The call to respond to the first corporate governance code issued in the UK namely the Cadbury Report, in 1992 (Marx, 2008; Miles & Jones, 2009).

In 1994, a commission was formed by retired judge, Mervin King, to establish a code on governance in South Africa. South Africa's corporate governance reforms now centre around four reports, namely the King Report on Corporate Governance (King I) issued in November 1994, the King Report on Corporate Governance for South Africa – 2002 (King II) issued in March 2002 (West, 2006), the King Report on Corporate Governance for South Africa – 2002 (King III) issued in 2009 and lastly the King Report on Corporate Governance for South Africa – 2017 (King IV) issued in November 2016.

King I was published in 1994. It was considered ahead of its time (Marx, 2008) as it set an international benchmark for standards and best practice (Jansen van Vuuren & Schulschenk, 2013). King I drew extensively on the Cadbury Report and similarly adopted a self-regulatory approach of 'comply or explain' (Mangena & Chamisa, 2008). This meant that companies which complied with the report needed to disclose their level of compliance and in instances where they did not comply, explain their reasons for non-compliance.

King II was drafted in 2001 and issued in 2002. Its effective date of implementation was 1 March 2002. Vaughn and Ryan (2006) and Marx (2008) described it as a more comprehensive report, which was built on the foundation laid by its predecessor. King II maintained its original stance and was not in favour of legislation which forced companies to comply with its recommendations but rather, it stayed true to the ethos of self-regulation (Miles & Jones, 2009). However, the report expanded on its 'inclusive approach' to corporate governance, recommending the introduction of 'triple bottom line' reporting to incorporate the economic, environmental and social aspects of a company's activities (Miles & Jones, 2009; Hendricks & Wyngaard, 2010).

The third report on corporate governance in South Africa came as a result of the new Companies Act of 2008 and changes in international trends in governance (IoDSA, 2009). King III, which was initially issued in 2009, promoted an integrated approach to governance and reporting, providing extensive guidance on integrated reporting and disclosures of governance-related matters (PwC, 2009; Maseko, 2015).

The most recent of the King reports, King IV, was published on 1 November 2016. The report replaced King III altogether and is applicable to all with financial years commencing on or after 1 April 2017 (IoDSA, 2016).

According to Deloitte (2016), King IV takes a bolder approach than King III insofar as:

- The report follows a principle- and outcome-based approach as opposed to being rule-based. This is consistent with current global opinions which advocate heightened accountability and transparency. It also recommends that practices ought to contribute to the performance and sustainability of a company.
- The report is resolute in its unyielding effort to reinforce the idea that corporate governance should be seen as a holistic set of arrangements that embraces ethical leadership, attitude, mindset and behaviour.
- The report continues to stress increased transparency and targeted disclosures in all areas.

From an application perspective, King IV is a framework which can be adopted across listed and unlisted companies, profit and non-profit as well as public and private entities (IoDSA, 2016). King IV steps away from the 'apply *or* explain' approach and recommends an 'apply *and* explain', relieving governing bodies from the burden of compliance by reducing the 75 recommended practices in King III to 16 basic principles. The 16 principles can be adopted by any company and are all necessary to substantiate the practice of corporate governance (IoDSA, 2016). The required explanation gives effect to each principle and enables stakeholders to make an informed decision on whether a company is well governed or not. The explanation also helps in shifting the focus of companies from a compliance mindset to a qualitative mindset, which encourages the achievement of objectives through careful consideration of the entity's circumstances (IoDSA, 2016; Piek, 2016). King IV also includes sector supplements that provide high-level guidance and direction on how the report should be interpreted and applied by a variety of sectors and organisation types. There is unfortunately no sector supplement for auditing firms (IoDSA, 2016).

1.2.2.6 Other corporate governance developments in the world

According to the the European Corporate Governance Institute (ECGI) (2020), there are many corporate governance codes around the world. A short summary of these codes is provided below. More details regarding the countries and their codes are set out in Annexure A.

In Austria, a corporate governance code was created as a set of rules and standards for the responsible management of companies. In Belgium there are corporate governance practices for listed companies. The Brazilian Corporate Governance Code is applicable to listed companies in Brazil. Corporate governance practices in Canada are shaped by legal rules and best practices. The Danish corporate governance regime is applicable in Denmark. In Finland, corporate governance is based primarily on the Finnish Companies Act (ECGI, 2020).

In France the corporate governance rules are mainly set out in recommendations contained in corporate governance codes and statutory provisions in the French Commercial Code. The German Corporate Governance Code 2019 is applied by listed companies in Germany. In Ghana the corporate governance is a combination of subsidiary legislation, statutory law and regulatory guidelines and directives. The Indian corporate governance framework is composed of statutes and regulations that require the supervision of multiple regulators. In Indonesia the general governance document of a company is its articles of association. Companies in Ireland are required to comply with both the Irish Corporate Governance Annex and the UK Corporate Governance Code. Companies in Japan are regulated by the national Companies Act. The Kenyan capital market is regulated by the Capital Markets Authority (CMA). In Luxembourg the main statutes on corporate governance include the European Union (EU) Market Abuse Regulation, the Companies Act and the Securitisation Act. The Nigerian corporate governance regime is characterised by a combination of a statutory framework and subsidiary legislation. The Norwegian Code of Practice for Corporate Governance includes important guidelines on the corporate governance of listed companies in Norway (ECGI, 2020).

In Poland, the Commercial Companies Code of 2000, which replaced the former Commercial Code of 1934, contains the general corporate governance rules applicable to companies, including listed companies. The Portuguese Commercial Companies Code contains the main legal sources of corporate governance rules in Portugal. Russia's corporate governance code and the listing rules of licensed stock exchanges contain the best practice provisions for listed companies in that country. The Singapore corporate governance regulatory framework is contained in certain mandatory rules. In Sweden, the statutory corporate law set out in the Swiss Code of Obligations is the main source of Swiss corporate governance regulation (ECGI, 2020).

1.2.3 Conclusion and critical link to the research problem

According to Lakshan and Wijekoon (2012), poor corporate governance increases the probability of corporate failure, even for organisations with good financial performance. Corporate governance is seen as a tool to combat corruption and unethical business practices which harm many countries' business image and reputation (Armstrong, 2003, as quoted by Rossouw, 2005).

Critical link to the objectives of the study

Corporate governance codes (like those mentioned above) were introduced because of corporate collapses, business failures and fraudulent financial reporting. However, regardless of all these codes, corporate failures continue to happen. It is therefore necessary to conduct a detailed literature review on the development of corporate governance codes in the UK, USA, Australia, the Netherlands and more specifically, South Africa. This review intends to identify the corporate governance principles that could be applied to auditing firms. It also provides grounds for the development of a checklist and the questionnaire which will be used in the empirical research.

The section below briefly discusses well-known corporate failures that took place as a result of weak corporate governance. A detailed discussion of corporate failures is presented in Chapter 3.

1.3 Corporate failures

The subject of corporate governance has received increasing attention in recent years due to a series of international and local corporate scandals (Maseko, 2015). In this study, it is important to understand when a corporate 'scandal' is classified as a corporate 'failure'. This is because there is a distinct difference between these two concepts. One should also be cognisant of the fact that corporate failures often occur as a result of audit failures. For this reason, it is important to distinguish between these concepts.

According to the Merriam Webster online dictionary, a 'scandal' is defined as "a circumstance or action that offends propriety or established moral conceptions or disgraces those affected with it" (Abdoul Fatahi, 2017). According to Abdoul Fatahi (2017), a scandal is generally associated or followed by disgrace upon the authors, shock on the part of the society and reprehensive action from social control agents. Hoffman (1999), as quoted by Abdoul Fatahi, (2017) says that a scandal is a public manifestation of a misconduct.

In contrast, a 'financial scandal' is "a situation or event that has occurred as a result of financial resources being employed in a morally questionable manner where there are serious consequences for third parties, which are widely known" (Toms, 2019: n.p.). Financial scandals may involve accounting and financial market manipulation, different types of fraud and the possibility of corporate bankruptcy. A scandal is created when certain behaviours have an effect on innocent third parties and the wider public. This behaviour could be morally questionable, but may not necessarily result in a scandal. Only once there is a widespread financial impact on individuals, causing them to lose material amounts of money and trust, does a scandal exist. Every year, investors lose enormous sums of money to fraud and corporate scandals (Okaro & Okafor, 2013). According to Toms (2019), the larger the collateral losses and social impact of such behaviour, the greater the public's appetite for regulation and reform.

According to Pearson (1987), an 'audit failure' takes place when an auditor indicates to the public that a client's financial statements are true and fairly presented when in fact they are not. Most corporate scandals often result in audit failures and the corporations fail as a result of fraud-related factors and behaviours (Muraina, Okpara & Ahunanya, 2010). In such cases, the investing public usually asks: 'Where were the auditors?' Audit failures are costly to the auditors, their clients and investors and to society as a whole (Okaro & Okafor, 2013).

It is said that auditors have more statutory rights than the police because they can exercise their powers and gain right of access to a company's books and any other document that they need to see, without a court order. Auditors can demand any information and explanation that they consider necessary to enable them to discharge their duties from company directors and officers. If anyone attempts to obstruct them, that person risks civil and possibly criminal penalties. Regardless of their powerful statutory rights and the huge social investment in auditing, auditors seem unable to deliver the promised accountability, surveillance, certainty, regulation and trust. Auditors often stand accused of covering up, and of injuring innocent third parties. According to

Sikka (2003), confidence in corporate governance and accountability is greatly affected by the audit failures.

For the purposes of this study, a ‘corporate failure’ is defined as an event or situation involving the use of financial resources, where questionable ethical behaviour arises when management misrepresents financial statements and auditors fail to discover or report this misrepresentation, which then becomes public knowledge.

Most of the well-known corporate failures have involved inadequate corporate governance and auditing processes and accountancy procedures that have been compromised (Maranga, 2018). The next section briefly discusses high-profile corporate failures in the UK, the USA, Australia, the Netherlands and South Africa.

1.3.1 Corporate failures in the UK

The 1980s saw an increase in the number of business scandals in the UK. This attracted criticism from the public, who felt that there was an apparent lack of controls on business conduct in the UK. There was considerable doubt about the efficacy of the existing system of self-regulation of companies listed on the London Stock Exchange (LSE). Questions were raised about the perpetrators of well-concealed frauds within large firms (Boyd, 1996). The sections below discuss the less well-known instances of corporate failure, followed by high-profile cases.

There were many low-profile fraud cases in the UK, such as Barlow and Clowes and Brent Walker, investment firms where the chief executives of the firms stole funds from investors. Another fraud case included the conglomerate Polly Peck, where corporate funds were illegally moved into offshore companies owned by the founder, Asil Nadir and the chief executive officer (CEO) (Boyd, 1996). There was also the scandal that involved stock manipulation by Blue Arrow. In the Guinness scandal, during the takeover battle for distillers, the business leaders inflated the value of the Guinness shares. The role of auditors in detecting fraud was debated after the collapse of the Bank of Credit and Commerce International (BCCI) (Boyd, 1996).

There were also many significant corporate failures in the UK. The corporate failure of Robert Maxwell came to a head on 5 November 1991. The case brought the media business empire, which had continued commercial activity for over 40 years, to an almost immediate halt. The following day the Swiss Bank Corporation contacted the Serious Fraud Office (SFO) in London declaring a £57.5 million loan that was awarded to a private Maxwell company was in default. The Swiss Bank Corporation disclosed that the demand to repay the loan was refused by Kevin Maxwell, the CEO of Maxwell Communications Corporations (MCC). The day after, MCC shares crashed, share dealings in Mirror Group Newspapers (MGN) and MCC, the other large public companies in Maxwell, were suspended on 2 December. The final collapse occurred when it was discovered that Robert Maxwell stole £933 million from his two public companies in order to support the share price of MCC (Clarke, 1993). The enormity of the fraud in this corporate failure, as well as the effect it had on pensioners, shareholders and employees, prompted the most far-reaching questions ever addressed on the subject of corporate governance in the UK (Clarke, 1993).

The corporate collapse of Barings Bank occurred in 1995. Before it came close to bankruptcy in 1980 as a result of a disastrous risky investment in Buenos Aires, Barings was a great force in the City of London in the 19th century. A consortium arranged by the Bank of England (Ziegler, 1988) bailed the bank out. The effect of poor internal control was evident in the case of Barings Bank, in which the general manager of the Singapore office engaged in illegal speculative trading on the Nikkei (the leading and most valued Japanese stock index), resulting in a loss of £827 million in 1995 without the knowledge of the management at the London headquarters (Coyle, 2010).

On 22 November 2014, Tesco admitted that it had overstated its profits by £250 million. Top brands would pay top dollar to secure a place for their product on Tesco's shelves. This was done in the form of rebates. However, increased competition from other grocery stores put Tesco under pressure. As a result, the fear of missing out on its volume-driven rebates grew even bigger. This ultimately led to management reporting inflated figures and Tesco's shares slumped to a 14-year low. Very shortly afterwards, the SFO announced it would launch a criminal investigation into the accounting practices of Tesco. The impact of the event was of such a magnitude that the FRC decided to examine the role of PricewaterhouseCoopers (PwC) and individual auditors (Adibi, Aziz & Nur, n.d.).

British Home Stores (BHS) failed in 2016. After falling into administration, the iconic chain closed for good. Thousands of jobs were lost and hundreds of stores were left vacant, many of them cornerstones of their high streets (Winter, 2019). BHS collapsed because it had not kept up with consumer trends. It made an annual loss of £70 million in 2013, according to records filed at UK's Companies House. The new owners were not able to turn their fortunes around due to a mixture of poor selling and not being able to collect enough cash from the portfolio of properties (Chu, 2016). Their auditors, PwC, were fined £10 million (reduced to £6.5 million) for the shortcomings during their audit work (Butler, 2018).

Many were surprised at the collapse of Carillion on 15 January 2018. Over the course of a weekend, the second biggest construction group in the UK went from going concern to compulsory liquidation. It came as a shock that Carillion had no real assets and more than £2 billion of debts and pension liabilities (Rogers, 2018). It was alleged that Carillion had not acted alone and members of parliament accused the Big Four auditing firms (Deloitte and Touche, KPMG, Ernst & Young and PwC), of contributing to this failure. These auditing firms, all of which had auditing, advisory or facilitation roles with Carillion, together earned £72 million in fees from the company in the decade before its failure (Sweet, 2018).

The Patisserie Valerie corporate scandal occurred in 2018 when the chain announced that it had discovered important and possibly fraudulent, accounting irregularities. After having been suspended, finance director Chris Marsh was arrested and is currently being investigated by the SFO and the FRC while former Patisserie Valerie auditors, Grant Thornton, are under investigation by the FRC (BBC News, 2019).

The Ted Baker collapse occurred in the same year, with the company announcing that its accounting mistake was actually almost three times as bad as first believed. During the investigation, audit firm Deloitte found that the valuation of the stock inventory of Ted Baker was overstated by £58 million. The initial projections of between £20 million and £25 million in 2019 (Jahshan, 2020) had been growing tremendously. KPMG had audited Ted Baker since 2001 and critics say the accounting mistake posed 'significant questions' for KPMG. Prem Sikka, a Sheffield University accounting professor who advised members of parliament on audit reform, and Rachel Reeves, president of the House of Commons business committee, called on the FRC to investigate. The 'serious questions' need to be answered about how, just months after the auditors had signed off the books, a massive hole in the balance sheet of had Ted Baker appeared (Daily Mail City & Finance Reporter, 2020).

1.3.2 Corporate failures in the USA

According to Becht, Bolton and Roell (2005), as quoted by Aziri (2014), scandals and major failures at USA corporations increased the importance of corporate governance. McKesson & Robbins was the first scandal of major importance in the USA, occurring in 1937, well before Enron and WorldCom. The public scrutinised the accounting profession for the first time when fraud was discovered at McKesson after 13 years, in 1937. This had a profound impact on the accounting profession (Shinde, Poznic & Buehne, 2010). Donald Coster, whose real name was Philip Musica, was the head of McKesson & Robbins. He had assumed a new name and identity to disguise his criminal record, which included bribery and grand larceny. Coster, together with his associates, formed a company and misappropriated $2.6 million. The accounting profession and the firm were shocked that the fraud continued undetected for such a long period of time (Previts & Thomas, 1996).

The 21st century saw some of the biggest and well-known corporate collapses, of which Enron was probably the most significant. According to Terry (2007), at that time Enron was the largest bankruptcy case in American history. Enron filed for bankruptcy in December 2001. The failure of Enron not only resulted in huge financial losses for shareholders but it also had an enormous impact on employees, who not only lost their jobs but also their pensions and savings. The number of big auditing firms in the USA was reduced from five to four, when the Enron auditors, Arthur Anderson disappeared overnight. This debacle raised questions about the credibility and the capacity of the audit profession at large.

However, Enron's bankruptcy was soon eclipsed by WorldCom (the nation's second largest long-distance telecommunications company), whose less sophisticated accounting fraud let to a larger restatement of earnings, a larger bankruptcy filing and equally far-reaching civil and criminal investigations (Brickey, 2003). In June 2002, WorldCom announced that in 2001 and in the first quarter of 2002, it had overstated earnings by more than $3.8 billion. The accounting manoeuvre responsible for the overstatement was characterised by the press as scandalous. They classified payments for other companies' communications networks as capital expenditures. Once again, doubt was cast over WorldCom's external auditor at that time, Arthur Andersen, and questions were raised as to why the auditors had not detected the fraud (Lyke & Jickling, 2002).

The Tyco scandal of 2002 reflected the company's unethical leadership. The company's corporate governance system was compromised when the CEO, Dennis Kozlowski, appointed his close associates in prominent positions. This allowed his associates to abet his unethical behaviour (Brickey, 2008). A weak control environment enabled Kozlowski and some other executives to perpetrate crimes of fraud, grand larceny, conspiracy, embezzlement, accounting conflicts of interest, excessive unethical personal spending and other questionable activities (Kay, 2002). Kozlowski and Swartz, Tyco's chief financial officer (CFO), were accused by the authorities of stealing \$170 million from Tyco and fraudulently selling \$430 million in stock options in 2002 (Brickey, 2008). PwC, which had been responsible for checking the financial reports of Tyco, had failed to identify Kozlowski's illegal financial transactions and therefore, his unethical business practices continued unchecked.

In 2008, there were several more business failures in the USA. Lehman Brothers, Madoff and American International Group (AIG) were among these. Lehman Brothers applied for bankruptcy on 15 September 2008. The 164-year-old corporation was the fourth largest USA investment bank. Its bankruptcy, which was spurred by the global financial crisis (Amadeo, 2020), revealed the use of a system known as 'Repo 105'. This system moved off-balance sheet assets and debt to make investors look more favourably on the bank's financial position. This meant that, although ostensibly still complying with USA generally accepted accounting principles (GAAP) limits, the bank was potentially misleading investors (Hail, Tahoun & Wang, 2017). Significant concerns were raised about the accounting practices of Lehman and the role that EY played in allowing these items to remain unchallenged and secret in its financial statements (Wiggins, Bennett & Metrick, 2015).

The \$65 trillion Madoff Ponzi system ruined the global economy. By soliciting billions of dollars of funds under false pretences, failing to pledge investor funds and misappropriating and shifting investor funds for the benefit of the company or for the benefit of others, without the knowledge or consent of the investors, Madoff initiated a scheme of defrauding customers (Federal Bureau of Investigation [FBI], 2009). Charges were brought against the auditors, Friehling & Horowitz (F&H), for false certification of having prepared the audit statements in accordance with GAAP.

In 2015, AIG (one of the biggest insurance companies worldwide) announced that it was being investigated for certain non-traditional reinsurance transactions. According to the management report that was released, as mandated by the SOX Act, certain members of senior management, including the CEO and CFO, overrode certain controls, transactions and accounting entries. The report noted a major deficiency in internal control over financial statements; this related to the valuation process and oversight of the AIG super senior credit default swap portfolio with respect to internal control concerns rather than valuation problems (Woods, Humphrey, Down & Liu, 2009). It was clear that AIG's control environment was not effective. The transactions and accounting entries that were manipulated were largely intended to achieve desired accounting results and were not properly accounted for in accordance with GAAP (Verschoor, 2005). AIG settled for nearly $1 billion and PwC, the auditor, settled for $97.5 million to assist the fraud (Lessambo, 2018).

More recently, General Electric (GE) accounting executive, Harry Markopolos, charged the firm with fraud in 2018, covering up to $38 million, worth 40% of its market value. KPMG had been GE's auditors since 1909 (de Luce, 2019). The shareholders voted to replace KPMG with a new independent auditor from 2020 onwards (Brasseur, 2020). It is claimed that KPMG's lack of independence contributed to the organisational failure of GE and the failure of the audit.

1.3.3 Corporate failures in Australia

HIH Insurance, One.Tel and Harris Scarfe are only a few of the corporate failures that have taken place in Australia (Mirshekary et al., 2005). The corporate collapses that took place in the early years of 2000 in Australia indicated a weakness in the accounting and auditing professions (Kavrar & Yilmaz, 2017).

On 15 March 2001, HIH Insurance collapsed, with debts estimated at AUD$5.3 billion. This resulted in a Royal Commission to investigate if there were any undesirable corporate practices as well as the extent to which the actions of directors, employees, auditors, actuaries and advisors contributed to the failure (Mirshekary et al., 2005). This corporate failure pointed out that there was a lack of corporate governance and that auditors played a role in the failure (Allan, 2006). According to du Plessis (2003), the HIH case was a perfect real-life example involving almost all aspects of bad corporate governance. Independence of the audit committee was clearly lacking, as the chairman and another member of the audit committee were previously senior partners of the auditors of HIH, Arthur Andersen (Leung & Cooper, 2003).

In the same year, the retailer Harris Scarfe was placed into voluntary administration after irregularities had been discovered, dating back six years. At that point, the company had been in operation for 150 years. In the beginning, it was alleged that Allan Hodgson, the CFO, had altered accounts to inflate the company's profits. These allegations were later confirmed when it was found that Hodgson had played the leading role in falsifying reports and accounts (Leung & Cooper, 2003). Harris Scarfe was one of the biggest corporate failures in Australia, with debts of AUD$265 million (Kavrar & Yilmaz, 2017). EY and PwC were sued by the Australia and New Zealand Banking Group (ANZ Bank) for the recovery of at least $70 million as the bank alleged that the auditors had been negligent (Leung & Cooper, 2003). According to Leung and Cooper (2003), the accountants were running two sets of books and the auditors failed to detect this.

Another scandal which occurred in 2001 was that of One.Tel, a group of Australian-based telecommunications companies. One.Tel decided to invest in its own telecommunications system, but this proved to be unsuccessful and resulted in financial strain. One.Tel manipulated its accounts to hide losses and to ensure that bonuses and salaries would continue to be paid (Allan, 2006). In 2001, a formal investigation was instigated by the Australian Securities and Investment Commission (ASIC) to investigate the potential breaches of the Corporations Law. These breaches included market disclosure issues, insider trading and possible insolvent trading. One.Tel was wound up on 29 August 2002 (Leung & Cooper, 2003).

In 2016, Australia witnessed the organisational scandal of Dick Smith Electronics. On 30 November 2015, Dick Smith Holdings Limited surprised the market by announcing that an inventory write-down of AUD$60 million was required, while the company's financial statements for 28 June 2015 were audited without adverse findings three months earlier. Inventory management is a retail company's lifeblood and can be used as a key risk area by auditors. Gray (2016) states that the inventory problem therefore occurred only over a short period of time; alternatively, it developed over a longer period of time and was ignored by the auditors. During the company's audits, Deloitte failed to recognise these inventory issues. This suggested that the auditors had failed to conduct their audits in accordance with the required standards and that they did not practice reasonable competence and care, instead engaging in misleading and fraudulent class action practices (Richards, 2019).

1.3.4 Corporate failures in the Netherlands

The rise and fall of Royal Ahold (Koninklijke Ahold NV) is an important event in terms of the corporate failures in the Netherlands. This large international retail grocery and food service company, with its headquarters in the Netherlands, was at its peak in 2001. Sales and profits of €66.6 billion and €1.1 billion, respectively were reported in 2001. Royal Ahold had almost 250,000 employees and operated in 5,155 stores in 27 countries. Ahold was established in 1887 as a family business by the Heijn family, but in 1948 the company went public. For over 100 years, it operated primarily in the Netherlands. In 1989, Ahold underwent a transition from a family-controlled to a management-controlled firm, which proved to be a very successful change. By November 2001, Ahold had a market capitalisation of €30.6 billion and generated over a 1000% return for its shareholders (de Jong, de Jong, Mertens & Roosenboom, 2007). Only two years later, in February 2003, shareholders lost most of their returns generated since 1989 and the company suffered a complete meltdown. All that was left was a company with an accounting scandal, a failed business strategy and litigation filings from across the world. The litigation included the $1.1 billion settlement between the USA shareholders and the firm itself, making this the fifth largest settlement in the USA and the largest involving a European company in the USA (Bickerton, 2005). Ahold became known as 'Europe's Enron' (*The Economist*, 2003; Benston & Hartgraves, 2002).

1.3.5 Corporate failures in South Africa

Well-known instances of fraudulent financial reporting and corporate scandals in South Africa include Masterbond, LeisureNet, Regal Bank, Unifer Bank, Saambou Bank, Tigon, Macmed, South African Airways, Randgold & Exploration, JCI and Fidentia (Marx, 2008), and more recently, VBS Bank, Steinhoff, Tongaat and Eskom. The most recent scandals involving auditing firms include KPMG, Deloitte, PwC and Nkonki, to mention only a few (Maranga, 2018).

In the recent past, South Africa has also experienced widespread allegations of political misconduct in what has been termed an attempt at 'state capture' through illegal collusion between private sector entities and politicians (Independent Regulatory Board for Auditors [IRBA], 2017; Thompson & Mahlaka, 2017, as quoted by Harber, 2018). 'State capture' is defined as a type of systemic political corruption in which private interests significantly influence a state's decision-making processes to their own advantage. In this regard, many allegations of collusion and misconduct in this state capture debacle have been laid against international organisations, notably, the audit firm, KPMG (Harber, 2018).

In 2017, in the face of mounting evidence of state capture, KPMG was accused of deliberate collusion and political meddling as well as performing sub-standard work in a number of engagements with organisations linked to state capture (Thompson & Mahlaka, 2017; Dludla, 2018 as quoted by Harber, 2018). Again, a lack of integrity, independence and professional scepticism by the audit firm was seen as the primary cause of the corporate failure (IRBA, 2017 as quoted by Harber, 2018). KPMG South Africa suffered the loss of significant audit clients, who chose to terminate their relationships with the firm. This corporate failure resulted in investigations by the Companies and Intellectual Property Commission (CIPC) and the Independent Regulatory Board for Auditors (IRBA) (Dludla, 2018 as quoted by Harber, 2018). According to Nkuhlu (2020), there was a complete breakdown of controls at KPMG. He states that compliance with King IV would have significantly reduced the chances of the KPMG disaster.

Another South African audit firm, Nkonki Inc., applied for voluntary liquidation in 2018 following a scandal involving a failed management buy-out transaction that was alleged to have been funded by parties linked to the state capture corruption allegations. As a result of these allegations against KPMG and Nkonki, the South African Auditor-General terminated its outsourcing of government audits to the two firms in April 2018, resulting in Nkonki seeking liquidation of one of its offices (Hill, 2018 as quoted by Harber, 2018).

The 2017 collapse of share price in Steinhoff International Holdings amidst allegations of extensive accounting and financial fraud (case ongoing) is another recent example of corporate failure. Yet again, questions were asked about why the auditors (Deloitte) did not raise concerns earlier and why prior years' financial statements had been signed off without qualification (Bowker, Bonorchis & Wild, 2017). Deloitte is now facing serious questions as to the quality and appropriateness of its prior audit work.

More recently, in 2019, Tongaat Hulett made headlines, which claimed that it was 'another Steinhoff' scandal. Tongaat stated that it would have to restate its profits, as they were not correct the first time. It seemed as though the auditors, Deloitte, had missed some important information and red flags.

According to Comrie (2020), a confidential investigation carried out in 2019, delivered a damning assessment of PwC's consulting work at Eskom, describing the fee structure as patently unlawful and stupendously egregious. Eskom issued PwC with a R95 million letter of demand. Eskom wanted the audit firm to pay back fees for a consulting deal that bore the signs of state capture. According to Eskom, PwC was taking the credit for work that they had already done, meaning that Eskom was paying PwC millions of Rands for work that they did not do, but merely duplicated.

These South African examples of corporate financial misconduct, especially where the auditor was implicated, have resulted in the public and the IRBA questioning the independence and professional scepticism of the South African audit industry, especially with regard to public interest entities and exchange-listed companies (IRBA, 2016, 2017 as quoted by Harber, 2018). It could be argued that there is a 'silver lining' to these revelations in that accounting or reporting irregularities were being identified, even if it was after the fact, and that corrective action was taken. The corporate sector in South Africa may need to take some tough measures itself if it wishes to maintain its reputation for transparency and good governance (Stoddard, 2020).

1.3.6 Other corporate failures

The corporate failures discussed below are to set the context for this study and to show that corporate failures happens all around the world.

The Satyam corporate scandal in 2009 was one of the worst in India's corporate history. The fraud amounted to about $1.7 billion and involved 7,561 false invoices and 13,000 'ghost workers'. According to the Securities and Exchange Board of India, the auditors, PwC failed to check financial records and relied on management's submissions in drawing up their 'independent' opinion (Maranga, 2018). This resulted in PwC being banned from auditing in India for two years. The former chairperson of Satyam was found guilty of falsifying accounts and income tax returns, of fabricating invoices and of collusion in inflating the company's reported gains. He was sentenced to seven years in prison (Maranga, 2018).

In Nigeria there have been similar cases, with Cadbury Nigeria's management overstating the company's financial position for several years to achieve their growth targets. This fraud added to the value of between ₦13 billion and ₦42-million (Maranga, 2018).

In Europe, other scandals included that of Parmalat in 2003. This Italian dairy products giant filed for bankruptcy when funds in excess of $18 billion were missing. Criminal charges, involving that of concealment of the financial condition of Parmalat to the public, were indicted on the directors and officers. Action was taken against Deloitte, Grant Thornton, Bank of America and Morgan Stanley by Italian prosecutors and the Parmalat bankruptcy estate. They alleged that these professional service providers assisted with the wrongdoing at Parmalat (Hughes & Lee, 2007).

In Germany, Holtzman, Berliner Bank and Babok were big corporate failures (Marx, 2008) whereas in France, Crédit Lyonnais, Vivendi and Société Générale were large scandals in which accounting fraud took place (Hsu, 2008).

1.3.7 Conclusion and critical link to the research problem

According to Aziri (2014), corporate governance is not simply good business, but it also helps to prevent fraud, corporate scandals and potential civil and criminal liability of the organisation. An organisation with good corporate governance boosts the organisation's reputation and attracts more investors, suppliers, customers and contributors. Corporate governance therefore produces a direct economic benefit to the organisation.

Unfortunately, corporate failures and fraudulent financial reporting have continued to shock the public over the years (Marx, 2008) and have had a direct effect on the auditing profession. The quality of audit is often questioned after financial scandals of public companies such as Sunbeam, Waste Management, Xerox or Adelphia, to mention only a few. The public is losing confidence in the work of the auditors and the profession at large (Boynton, Johnson & Kell, 2006, as quoted by Teck-Heang & Ali, 2008).

Critical link to the objectives of the study

Poor corporate governance practices, 'creative' accounting, fraudulent financial reporting, auditor inefficiency and independence issues are some of the common factors present in corporate scandals (Marx, 2008). This study explores how the lack of corporate governance has contributed to some of the worst financial corporate failures in the UK, the USA, Australia, the Netherlands and South Africa, as well as exploring whether weak governance practices at auditing firms have contributed to corporate failures or to the inability to detect such failures. Through a literature study, the most important principles of corporate governance are identified to assist in providing guidelines for corporate governance practices and oversight structures for auditing firms in South Africa.

Audit quality and an audit firm's ability to continuously provide audit services to the public is influenced by the corporate governance of the audit firm (La Rosa, Caserio & Bernini, 2018). It is clear from the literature that a lack of corporate governance has contributed to some of these corporate failures. Many of these corporate failures have resulted in audit firm failures, or at the very least, in damage to the reputation of the auditing firms. The next section briefly discusses audit firm failure.

1.4 Audit firm failures

Audit firm failures refer to the failure of the auditing firm that was involved in a financial scandal or corporate failure, such as Arthur Andersen in the case of Enron. The definition of a corporate failure previously used in this study is applied to that of an auditing firm, with an 'audit firm failure' being defined as follows:

> *An event or situation involving auditing firms, where questionable professional and ethical behaviour arises, which then becomes the knowledge of the broader public, thus affecting the reputation of the auditing firm, which could ultimately result in the closure of the firm.*

In the case of Enron, the external auditors, Arthur Andersen, were also the financial consultants to the entity. This created a conflict of interest in terms of their auditing role and resulted in them not giving a fair and true audit opinion on Enron's operations. The scandal led to the failure of Enron and, subsequently, the failure of the audit firm itself (Maranga, 2018).

There are also many corporate financial scandals and audit failures where the auditing firms did not fail; however, they suffered massive reputational damage—as can be seen in the examples of the KMPG scandals in South Africa.

Critical link to the objectives of the study

A literature review was conducted to determine the impact of weak corporate governance practices at auditing firms on the reputation and sustainability of the auditing firms as well as their role in possible audit firm failures. This review supports the research problem, to provide guidelines on corporate governance practices and oversight structures for auditing firms in South Africa, in order to minimise the possibility of corporate failures and audit firm failures.

The research gap in this study is formed by the fact that very little research has been conducted to date on the corporate governance of auditing firms. As literature states, it is the lack of corporate governance that could lead to corporate scandals and thus the question is: 'Could corporate scandals and audit failures be prevented if better corporate governance practices were to be implemented in auditing firms?'

1.5 Corporate governance in auditing firms

1.5.1 Introduction

The audit profession takes on the responsibility of detecting and reporting fraud as well as raising doubts about their clients' ability to apply and disclose corporate governance matters (Teck-Heang & Ali, 2008). Auditing firms regard themselves as the 'intellectual hub' of corporate governance advisory, yet very few have a credible and compliant board of directors. To comply with corporate governance, the auditing firms should have a board of directors with a majority of non-executive directors, appropriately balanced in terms of the mix of competencies (Aberian, 2019). At present, the corporate structures of auditing firms are flawed. Some auditing firms argue that they need not comply with the codes of corporate governance as their business model is based on 'partnership'

(Aberian, 2019). According to Nkuhlu (2020), all auditing firms need to appoint independent, non-executive directors (INEDs) and place risk and ethics under their oversight.

Corporate governance disclosures of listed companies is a topic that has been researched and explored to some extent over the years (see, for example, Bauwhede and Willekens (2008), Collett and Hrasky (2005), Markarian, Parbonetti and Previts (2007) or Parum (2005)), however, very little empirical evidence exists on corporate governance practices and disclosures of auditing firms (La Rosa et al., 2018).

The sections below explain the legislation, codes and regulation which offer guidelines to auditing firms with regard to corporate governance.

1.5.2 South Africa

According to the Institute of Directors in Southern Africa (IoDSA) (2016), King IV aspires to apply to all organisations, regardless of their form of incorporation. A main objective of King IV is to make it accessible and fit for application in different types of organisations and sectors. This implies that even auditing firms should apply King IV, yet, taking into consideration the recent corporate failures in South Africa, there is clearly a lack of application of King IV by South African auditing firms. According to the chairman of KPMG South Africa, Professor Wiseman Nkuhlu (2020), KMPG is one of very few, if not the only, audit firm to apply King IV.

The Audit Profession Act (APA) does not have a specific chapter providing information or guidance on the governance of auditing firms. Chapter II, Part 4 provides details on the governance of the regulatory board, which in this case is the IRBA.

In 2009, the International Auditing and Assurance Standards Board (IAASB) issued the ISQC 1. The ISQC 1 addresses "*Quality Control for Firms that Perform Audits and Reviews of Financial Statements and Other Assurance and Related Services Engagements*". It is applicable to all auditing firms. However, the ISQC also makes little specific reference to audit firm corporate governance structures and practices (IRBA, 2018). In South Africa during 2018, the IRBA issued a call to auditing firms to release transparency reports in order to disclose the relevant internal information to the public. To date, the release of such transparency reports had been voluntary for auditing firms (IRBA, 2018).

1.5.3 Internationally

Sir Donald Hood Brydon is a British businessman who is the chairman of the Science Museum Foundation, the Sage Group and the Charities Chance to Shine. He is also the author of the Brydon Report, published by the UK government. The report discusses the quality and effectiveness of audit. According to the Brydon Report, there are certain principles that provide a framework for the behaviour of auditors beyond simply following standards and the law (Brydon, 2019). The Brydon Report also makes no specific reference to audit firm corporate governance. The emphasis is placed on the individual auditor.

As mentioned in section 1.2.2.1, there is only one specific corporate governance code in the world for auditing firms, namely the Audit Firm Governance Code in the UK. One of the objectives of this Code is to enhance auditing firms' transparency reports. Regulators and standard-setters state that transparency about the corporate governance of auditing firms will reduce information asymmetry between auditing firms and the public and it will maintain high-quality audit services, thereby adding to the stability of the capital market (Deumes, Schelleman, Bauwhede & Vanstraelen, 2012). According to the CEO of the FRC, Stephen Haddrill, the UK Audit Firm Governance Code enhances the trust and confidence of the public and investors in the value of audit services. He added that the Code reduces the risk of firm failure by contributing to the reputation of auditing firms and promoting greater transparency (ICAEW, 2017). The Code also consists of other corporate governance principles which auditing firms should implement, namely, (1) Leadership, (2) Values, (3) INED, (4) Operations, (5) Reporting, and (6) Dialogue (FRC, 2016).

To enhance transparency, auditing firms are expected to release any information that might affect market confidence (Kumar & Zattoni, 2014; Mallin, 2002; OECD, 2015b). Transparency reporting (or similar reporting) is usually mandatory for auditing firms which audit public interest entities (PIEs). Jurisdictions where this is the case include the European Union, Japan, Australia, the UK and New Zealand, among others.

In 2013, Australia mandated that larger auditing firms of significant entities had to release a transparency report that makes specific reference to the audit firm's internal governance systems (Fu, Carson & Simnett, 2015). The release of transparency reports has only been mandated in a few countries. The majority of the research that is available was conducted in Europe, where auditing firms have been subject to mandatory transparency reporting requirements since 2008 (Deumes et al., 2012; Pivac & Čular, 2012).

In 2015, the IAASB issued the *Invitation to Comment (ITC): Enhancing Audit Quality in the Public Interest: A Focus on Professional Scepticism, Quality Control and Group Audits*, which introduced the topic of transparency reporting. According to the ITC, firms are required to release transparency reports that provide information on certain elements of the firm and its operations (IRBA, 2018). The IAASB (2014) states that audit firm transparency reports will assist third parties, such as the public and users of the audited financial statements, to understand the characteristics of the individual auditing firms and the drivers of audit quality in those firms. They further state that auditing firms can display to the public their approach to audits and therefore compete on aspects of audit quality by issuing transparency reports (Deumes et al., 2012). The call for greater transparency and disclosure by auditing firms is supported by the high-profile audit firm failures (such as the demise of Arthur Andersen) and the lack of confidence in the financial market in the post-global financial crisis era (Huddart, 2013).

According to Aberian (2019), a new and different regulatory framework is needed for the auditing profession as well as new legislation and a new and effective independent regulatory board. It would seem that the time is ripe for corporate governance guidelines to be developed specifically for auditing firms in South Africa, to ensure that all stakeholders and public interests are protected and that corporate failures are kept to a minimum.

Critical link to the objectives of the study

Based on the above discussion, it is clear that the corporate governance of auditing firms is an area that requires extensive research. This study investigates the current corporate governance structures at auditing firms as well as determining the corporate governance expected to be implemented by South African auditing firms based on the literature review.

1.6 Background to the research problem

The research problem was identified from a gap in the body of knowledge. The literature proved to have limited information which made reference to corporate governance at auditing firms, and also indicated that there is only one corporate governance code for auditing firms in the world. Auditing firms in South Africa only started to implement King IV after various corporate scandals and corporate failures occurred in recent years in South Africa. In these scandals and corporate failures, it was specifically the auditing firms that were implicated. This led to mounting public interest questioning the auditing industry in South Africa (IRBA, 2016, 2017).

The research problem is supported by the following literature. A study conducted by Uzun et al. (2004) examined how the occurrence of fraud was affected by the company's governance features and various characteristics of the board of directors. The results indicated that the structure of committees and the composition of the board of directors had a significant effect on the occurrence of corporate fraud. The authors found that the more INEDs on the board, the less likely the occurrence of corporate fraud.

Another study conducted by La Rosa et al. (2018) found that investors believed that transparency reports provide meaningful information about audit firm quality and independence. A 2019 study by the same authors suggests that transparency on corporate governance issues by all organisations, including auditing firms, contributes to the sound development of financial markets.

According to DeFond and Zhang (2014), further research is needed on the characteristics of auditing firms such as the type of ownership structure, audit quality control systems, compensation schemes and governance systems. These characteristics would provide important insight into factors that affect auditor competency and incentives. Transparency reports and the information they contain would allow researchers to examine these characteristics.

A study conducted by Fu et al. (2015) on the governance structures of auditing firms in Australia found that the partners were majority members of the board of directors and three auditing firms (Grant Thornton, BDO and Brisbane and Moore Stephens from Melbourne) indicated that they had an independent chairperson. The information about local board composition was not specified in the transparency reports. Relatively few auditing firms disclose further information on their boards.

As stated by the IRBA (2017), a lack of independence, integrity and professional scepticism by the audit firm are seen as the primary cause of corporate scandals. It is also evident from the integrated reports and transparency reports of the large auditing firms within South Africa that the governance structures of most auditing firms do not adhere to the King IV requirements in terms of board composition and independence. According to Nkuhlu (2020), corporate failures are a consequence of auditing firms becoming commercial enterprises driven by revenue and profits for the partners. He states that a lack of independence and 'cosy' relationships with clients result in corporate failures.

From the above studies one can see the significant role that independence plays in corporate governance. This is also supported by the various corporate governance codes that have independence as one of the principles that should be applied in order to practice good corporate governance (more detail to be provided in Chapter 2). It is here that the gap has been identified within the literature on the lack of corporate governance within auditing firms and the impact that this has had on public trust.

1.7 Research problem

Although corporate governance issues have been thoroughly debated over the years and various studies have been conducted on the topic, virtually no research has been conducted on the corporate governance of auditing firms. It is essential that auditing firms understand the responsibility they have to implement corporate governance and appoint an independent governance structure. They need to understand the value it can add to the organisation and all stakeholders. Currently in South

Africa there is no legislation or code that regulates the corporate governance of auditing firms. Auditing firms are also not required by any law to disclose their corporate governance structure and application in any report. Auditing firms are encouraged by IRBA to issue a transparency report in which they disclose corporate governance structures and application, but this is not compulsory in South Africa. Moreover, the information issued in these transparency reports is limited and often only focuses on audit quality, and not governance. It is nonetheless clear from the limited amount of information disclosed that auditing firms do not apply corporate governance principles, specifically with regards to independent governance structures.

As mentioned above, corporate governance addresses issues relating to ethics, accountability, transparency and disclosures as well as organisations' social and environmental impact (Raemaekers, 2014; IoDSA, 2009). Should auditing firms apply better corporate governance practices and principles, it is expected that the incidence of corporate scandals and failures would lessen. The research problem is formulated below.

Auditing firms in South Africa do not have effective governance structures and are not applying corporate governance practices and principles. This is evident from the amount of corporate scandals and failures that have taken place recently and the auditor implication in these scandals. The current corporate governance code in South Africa, King IV, does not have a specific sector supplement for auditing firms. Therefore, this study aims to provide guidelines on corporate governance practices and oversight structures for auditing firms in South Africa which could possibly be included as a sector supplement in future King Code iterations.

The following literature supports the research problem:

- **Auditing firms are in the spotlight**
  Recently in South Africa, the number of global corporate scandals has risen and this has led to huge financial losses. It has also led to increased calls for greater auditor independence and a better understanding of the role of the auditor. Most of the South African scandals have involved failed corporate governance and auditing processes and compromised accountancy procedures (Maranga, 2018).

- **Corporate scandals and corporate governance**

  Poor corporate governance practices, fraudulent financial reporting, 'creative' accounting as well as auditor inefficiency and independence issues, which are practiced by auditing firms, have all contributed to international and local corporate scandals (Marx, 2008).

- **Lack of literature and empirical research on the corporate governance of auditing firms**

  While many studies have explored the determinants of corporate governance disclosures of listed companies (e.g. Bauwhede & Willekens, 2008; Collett & Hrasky, 2005; Markarian et al., 2007; Parum, 2005), there is very little evidence on corporate governance disclosures of auditing firms (La Rosa et al., 2018).

- **Failure to apply corporate governance in auditing firms**

  To comply with corporate governance, the auditing firms should have a majority of non-executive directors, with a mix of competencies on the board of directors (Aberian, 2019). Currently, most auditing firms do not have good corporate structures. Some auditing firms use a 'partnership' business model, arguing that they do not have to comply with the codes of corporate governance (Aberian, 2019). According to the South African Auditing Profession Trust Initiative (SAAPTI) (2020), there is a need to set out the principles and best practices that the auditing firms should apply to achieve good governance (setting the 'tone at the top'). There should be a set of principles for best practice on the effective governance of ethics within auditing firms. Governance structures for auditing firms should be clearly defined. According to SAAPTI (2020), there is uncertainty as to whether auditing firms have ethical leadership and effective structures to govern ethics and whether firms are structured in a way that encourages them to act as good corporate citizens serving the public interest.

- **The benefit of transparency reports for auditing firms**

  Transparency reports provide all stakeholders with insights into an audit firm's corporate governance processes and structures (IRBA, 2018).

1.8 Research objective

The objective of this study is to provide guidance to auditing firms on corporate governance practices and structures that should be implemented to establish oversight on the corporate governance of the auditing firms.

More specifically, the study seeks to add to the existing body of knowledge as follows:

- To examine the development of corporate governance in the UK, USA, Australia, the Netherlands and more specifically, in South Africa. This analysis is necessary to identify the corporate governance principles that are applicable to auditing firms and provide grounds for empirical research on the application and disclosure of corporate governance within auditing firms in South Africa (Chapter 2);
- To make a comparison between the UK audit firm governance code and King IV to identify the similarities (Chapter 2 and Annexure I);
- To explore how the lack of corporate governance has contributed to some of the worst financial corporate failures the UK, USA, Australia, the Netherlands and South Africa and establish whether auditing firms contributed to these failures. Through this literature review, the most important principles of corporate governance are identified to provide guidelines on corporate governance practices and oversight structures for auditing firms in South Africa (Chapter 3);
- To determine the current legal and governance structures in auditing firms as well as indicating the corporate governance that should be implemented by auditing firms (Chapter 4);
- To perform a content analysis of the integrated reports and/or transparency reports of large and medium-sized auditing firms with 20 or more partners and determine what is disclosed on their corporate governance practices (Chapter 5);
- To formulate a questionnaire based on the literature and the current corporate governance practices at auditing firms to determine what the current practice at auditing firms. The questionnaire will also obtain the expert opinions of the CEO's of the top nine auditing firms with regards to corporate governance at auditing firms (Chapter 5).

These objectives are achieved through a literature review (Chapters 1 to 4) and a content analysis and empirical study (Chapter 6) based on the research methodology selected for this study (Chapter 5).

The cut-off date for the study is set at 31 August 2020. Any developments after this date will be addressed in future research.

1.9 Study layout

The study is divided into seven chapters, summarised below.

Chapter 1 – Introduction and Study Overview

This chapter sets out the background to the study and the aspects that prompted the concerns over corporate governance in auditing firms. The background to the research problem and the motivation for the study are also explained.

Chapter 2 – Corporate Governance

This chapter discusses the developments in corporate governance in the UK, USA, Australia, the Netherlands and South Africa. Acts, standards and codes on audit firm governance are examined through a detailed literature review.

Chapter 3 – Corporate Failures and Audit Failures

This chapter investigates the corporate failures in the UK, USA, Australia, the Netherlands and South Africa.

Chapter 4 – Current Corporate Governance Structures and Practices at Auditing firms

This chapter considers the legal and corporate governance structures of auditing firms. It also addresses concerns over corporate governance practices at auditing firms and suggests solutions from the literature.

Chapter 5 – Research Methodology

This chapter describes the theoretical framework, the research design and research methodology applied in this study. The chapter also describes data collection and analysis techniques, sampling and ethics applied in this study.

Chapter 6 – Empirical Study, Analysis and Findings

Chapter 6 presents the qualitative findings from the content analysis and compares these to the quantitative findings from the questionnaires. The results are analysed and discussed.

Chapter 7 – Conclusion and Areas for Future Research

Based on the findings from the literature and the results of the empirical study, conclusions and inferences are drawn and recommendations are made. Possible areas for future research are also identified.

1.10 Conclusion

This chapter provided a background on corporate governance and its impact on corporate failures, with a specific focus on the involvement of auditing firms in these failures. The chapter also explored the various corporate governance codes that have been adopted in the UK, USA, Australia, the Netherlands and South Africa. The literature indicated that a lack of corporate governance could lead to corporate scandals and corporate failures. Corporate governance thus plays a vital role in protecting the public interest. The literature also revealed that there is no specific corporate governance code that governs the corporate governance of auditing firms in South Africa. As a result, many auditing firms lack sound corporate governance practices and principles. It was posited that this could be the cause of many corporate failures and that should auditing firms implement a corporate governance code, corporate failures and audit firm failures would decrease. The corporate governance expectations for auditing firms were also discussed in relation to transparency reports. The research problem was explained and the research objectives were formalised. The chapter concluded with a summary of the study layout.

The next chapter explores the development of corporate governance in the UK, USA, Australia, the Netherlands and South Africa.

Chapter 2: CORPORATE GOVERNANCE

2.1 Introduction

This chapter contains a literature review of corporate governance and related theories in the context of corporate governance developments in the UK, USA, Australia, the Netherlands and more specifically, South Africa. Then, literature addressing the corporate governance of auditing firms is discussed. Thereafter the principles that are applicable to auditing firms are identified to provide grounds for the empirical research on the application and disclosure of corporate governance within auditing firms in South Africa.

The word 'governance' is derived from the Latin verb *gubernare*, which is in turn derived from the Greek word, *kubernaein*, which means 'to steer'. As can be seen from its etymology, governance refers to the way in which a group of people or a state is governed, directed or controlled (Tamayao, 2014).

According to Cochran and Wartick (1988), the term 'corporate' covers multiple aspects relating to theories and practices of boards of directors and their executive and non-executive management. The Institute on Governance (2020) indicates that governance consists of the following set of principles, which also frequently recur in much of the literature, namely, legitimacy and voice, direction, performance, accountability and fairness. These principles are also supported by various other authors and institutions that include them in their definitions of governance (Ally, 2016; Aziri, 2014; Bendixen & Thomas, 2000; Clarke, 2004; Cochran & Wartick, 1988; Frederick, 2000; Fung, 2014; Gillan & Starks, 1998; IoDSA, 2016; Millar, Eldomiaty, Choi & Hilton, 2005; Monks & Minow, 1995; Ntim, Lindop & Thomas, 2013; O'Donovan, 2003; OECD, 2015a; Patel, 2013; Rossouw et al., 2002; United Nations Economic and Social Commission for Asia and the Pacific, 2009; World Bank, 2016).

These principles are discussed in greater detail below.

i. Legitimacy and Voice

This refers to participation and consensus orientation. Participation means that a decision-making voice should be available to all individuals. This could be directly, or through the institutions that represent their intention. Board participation is built on freedom of speech and association as well as the opportunity to constructively participate. Consensus orientation refers to the manner in which the board of directors ensures that decisions on policies and procedures are made in the best interests of the group (Institute on Governance, 2020).

This view is supported by Cochran and Wartick (1988), who state that governance concentrates on the relationship between boards, top management, regulators, stockholders, auditors and other stakeholders. Monks and Minow (1995) agree, contending that corporate governance is the relationship among various participants in determining the direction and performance of corporations. The FRC (2019) also supports these principles, stressing that companies do not exist in isolation. Successful and sustainable businesses create prosperity and provide employment. In order to be a sustainable organisation, successful relationships have to be formed by the directors and the stakeholders. If these relationships are built on respect, mutual benefit and trust, they will be successful.

According to Fung (2014), a corporate governance framework based on commitment to effective corporate control, transparency and accountability can restore trust between governing bodies and stakeholders by enabling informed decision-making for shareholders, potential investors and stakeholders in relation to the company's operations. This will, in turn, enhance performance and improve corporate reputation and goodwill (Ntim et al., 2013). According to Cadbury (2004), as cited in Clarke (2004), the overall purpose of corporate governance is to align the interests of corporations, all stakeholders and society as closely as possible.

ii. Direction

This principle refers to having strategic vision in that governance and human development are a long-term perspective for leaders of organisations and the public. Direction also takes into consideration what is needed for such development. It is important to also consider the historical, cultural and social complexities in which that perspective is grounded (Institute on Governance, 2020).

This view is supported by the World Bank (2016), which states that corporate governance concerns the system by which companies are directed and controlled. The same definition is echoed by Smerdon (1998) as quoted by Rossouw et al. (2002).

iii. Performance

This refers to responsiveness, effectiveness and efficiency. To achieve this, organisations should serve all their stakeholders and achieve their objectives while making use of all their resources (Institute on Governance, 2020). According to O'Donovan (2003), corporate governance serves the needs of shareholders and stakeholders by directing and controlling management activities, through an internal system of policies, processes and people. The author also emphasises that integrity, accountability, objectivity and business acumen play an important role. A healthy board culture, legislation and reliance on external market place commitment contribute to sound corporate governance (O'Donovan, 2003).

This view is supported by Stemberg, Hess, Schleifer, Vishny, Tricker, Cannon, Keasey and Wright, as cited by (Aziri, 2014), who agree that any actions that affect the interests of shareholders should always be supervised and controlled. They state that corporate governance includes the control and administration of human resources and the company's capital.

iv. Accountability

This involves being accountable and transparent. Public and institutional stakeholders trust the decision-makers in government, the private sector and civil society organisations to be accountable. A free flow of information is key in ensuring transparency. It is also important that the parties which are concerned with the institution, their processes and information have access to adequate information to understand and monitor the institutions (Institute on Governance, 2020). The World Bank (2016) confirms that governance is about accountability; owners and companies are able to build trust and confidence when they are accountable.

The importance of transparency and accountability has been widely recognised by both academics and market regulators. These are important elements of a robust corporate governance regime (Fung, 2014). These two traits assist governing bodies to minimise agency problems by reducing information asymmetry between those charged with governance and corporate stakeholders and to enhance goal congruence by aligning the goals of the company with those of society (Ntim et al., 2013).

Transparency also suggests that information is easily available and accessible to stakeholders who are affected by the decisions taken by the governing body and their enforcements (United Nations Economic and Social Commission for Asia and the Pacific, 2009). Patel (2013) argues that transparency creates and maintains a level of openness and non-secrecy of information in companies. It is an effective way of protecting the interest of stakeholders by promoting disclosure of non-financial information necessary to hold governing bodies accountable for the decisions that directly or indirectly affect them (Frederick, 2000; Fung, 2014).

Accountability is the obligation of a company to answer for and accept responsibility for its activities and disclose the outcomes in a manner that is transparent to all stakeholders (Patel, 2013). Accountability cannot be achieved without transparency; as such, the two concepts are inseparable, for if a company's governance system is committed to transparency, it will promote accountability as well (Millar et al., 2005; Ally, 2016).

The OECD (2015a) states that the integrity of businesses and markets is essential to the health and stability of the global economy. It is therefore important to ensure sound corporate governance through rules and practices which promote transparency and accountability in companies.

v. Fairness

The fairness principle makes reference to equity and the rule of law. Fairness means that every individual has an opportunity to maintain or improve their well-being. This is also supported by King IV (IoDSA, 2016), which states that if a governing body strives towards an ethical culture, effective control, good performance and legitimacy, good corporate governance will follow. It is also important that the legal frameworks, such as the human rights laws are enforced impartially. Gillan and Starks (1998) concur, stating that corporate governance is the system of laws, rules and factors that control operations at a company. A Commonwealth Association for Corporate Governance report states that the governing body should govern the organisation with integrity (Bendixen & Thomas, 2000). The FRC (2019) maintains that a company's culture should be responsive to all stakeholders and shareholders and should promote integrity and openness. According to the United Nations Economic and Social Commission for Asia and the Pacific (2009) transparency occurs when the governing body makes decisions that are consistent with established regulations and laws.

From the above discussion, the following corporate governance definition has been formulated and is used in this study:

> *Corporate governance is a set of responsibilities and practices instituted by the governing body in order to direct a company to achieve its strategic objectives while remaining sustainable, accountable and transparent and acting in the best interests of all stakeholders*.

The above definition is applicable to both corporate entities as well as auditing firms.

What is important about governance structures, is that they have to be clear and understood by all individuals in order to be effective. Such structures are effective when individuals feel that their motives count. Corporate governance practices are diverse and differ across the world. Economic, political and legal backgrounds as well as the history and culture of a country further increase the diversity of governance structures (Clarke, 2004).

It is widely recognised that corporate governance can contribute to the long-term sustainability and economic success of corporations (Armstrong, 2003, as quoted by Rossouw, 2005). Rossouw (2005) agrees, stating that corporate governance can improve the reputation of companies and enhance corporate responsibility, which attracts foreign and local investors. Good corporate governance deters unethical business practices and corruption, which are sure to have a negative impact on the reputation of an organisation. The benefits of corporate governance justify the implementation of sound corporate governance structures (Armstrong, 2003).

From the above definitions, it is clear that corporate governance is about the 'tone at the top'. ISQC 1 has been substantially enhanced to improve the robustness of a firms' governance and leadership.

In particular, it addresses the expected behaviour of firm leadership in setting the tone at the top. For this reason, this study emphasises the tone at the top of auditing firms' governance and leadership structure. This study does not focus on audit quality, as many studies, codes, acts and legislation have already covered this topic.

Theory of corporate governance is frequently described in terms of two apparently opposing models: the shareholder model and stakeholder model. The differences between these two models reflect different theories of the corporation (West, 2006). The following section discusses these two theories of corporate governance.

2.2 Theories of corporate governance

2.2.1 Introduction

The agency theory, which arose when the ownership of companies became separated from their control, resulted in the birth of the concept of corporate governance (Rossouw et al., 2002). According to Corfield (1998), for the last 150 years, the purpose of the corporate structure has been to maximise profit purely to increase shareholder wealth. More recently, however, the focus has shifted to include social considerations as awareness has grown of interdependencies created between various groups, with which the corporation has a legitimate concern. These groups include customers, suppliers, employees and broader society (Corfield, 1998).

Corporate governance was subsequently introduced to ensure that companies were controlled by their owners in a way that served the best interests of all stakeholders (Rossouw et al., 2002). Rossouw (2005) supports this by stating that the governing body is obliged to be accountable to stakeholders and shareholders. The ethical standards of the company are conveyed in the way the company treats its stakeholders. In other words, the moral sensitivity of the company is reflected in the way in which stakeholders are engaged with (Rossouw, 2005).

From the above discussion, it is clear that there are two opposing theories in corporate governance, namely, the agency theory, also referred to as the shareholder theory, and the stakeholder theory. These two opposing theories are discussed in detail in sections 2.2.2 and 2.2.3. Another theory which is also discussed in this section is that of the one-tier and two-tier board structures. More about this theory will be discussed in section 2.2.4 below.

2.2.2 Shareholder theory

The shareholder theory and agency theory is in harmony, and therefore this section could refer to any of the two terms. Theory agency developed by Jensen and Meckling in 1976 is defined as a contract whereby one party (the principal) hires another party (the agent) to perform a service on their behalf. Managers operating to further their own interests as agents are unlikely to maximise returns for shareholders (principals) unless adequate governance mechanisms are introduced to protect shareholders' interests (Jensen & Meckling, 1976). The agency problems resulting from the separation of ownership and control, if left unchecked, can result in firms being run less efficiently, thereby reducing their value (Shleifer & Vishny, 1997). An important assumption of the agency theory is that managers are extrinsically motivated and, in the absence of incentives and controls, will expropriate wealth from the principal for their own benefit (Dedman, 2016).

Heath and Norman (2004) refer to the above as the shareholder theory. Shareholder theory deals with circumstances in which one person, the principal, wishes to compel another, the agent, to perform a function that is in the interests of the principal, but not necessarily of the agent. This effect can be accomplished either by moral persuasion or by offering rewards (Heath & Norman, 2004).

The shareholder model takes the view that the owners of the company (the shareholders) aim to supply consumers with products or services for the benefit of themselves, as owners; they are therefore expected to be responsible and accountable. This view is dominant in the USA and most English-speaking countries. The shareholder model includes the fundamental right to individual private ownership and the belief that economic efficiency is achieved by market forces. The right to individual private property lends itself to self-interested behaviour, which leads to the key issue in this model, such as the conflicting interests of owners and managers (West, 2006).

The shareholder model holds that the corporation is an extension of its owners and is ultimately responsible to those owners (Andreasson, 2011). Key assumptions of the shareholder model include the inviolability of private ownership. This implies that the shareholders who own the company have exclusive rights to determine company priorities and they also have rights to any profit generated (West, 2006). This model needs to resolve potential conflicts of interest between owners (principals) and managers (agents) (Pratt & Zeckhauser, 1985). It does so in most cases by linking managerial rewards to corporate performance, measured by share price, exercised by means of stock options (Letza, Sun & Kirkbride, 2004). This generally precludes any serious consideration of market interference in achieving the goals of the corporation, such as requiring corporations to consider matters beyond the financial 'bottom line' (Andreasson, 2011).

There is also ample opportunity for executives to hide information, as demonstrated in the Enron, Steinhoff, VBS and Tongaat scandals, to name only a few, or to frustrate shareholder efforts to obtain access to information. Compounding the issue is the fact that when it comes to regulation and control, shareholders frequently face their own collective action crisis. It requires time, effort and money to keep an eye on management and criticise their decisions. Generally, when there is one single dominant shareholder, that person would find it in their interest to accept such charges (Heath & Norman, 2004).

It is widely accepted that good corporate governance systems are required to alleviate the problem that occurs as a result of corporate ownership separation and control. Based on this, companies with stronger governance systems, such as more autonomous boards, are likely to provide their shareholders with greater returns than those with weaker governance structures (Christensen, Kent & Stewart, 2010).

Corporate governance mechanisms have the primary purpose of minimising or addressing these collective action issues. If actions are entirely measurable and all other information is common knowledge, then it is easy to create such incentive schemes. The main-agent framework becomes interesting only when there is a certain asymmetry of information between the principal and the agent. Senior executives and shareholders or board members have this asymmetry. These asymmetries generate the opportunity for opportunistic behaviour, where executives can use their intimate knowledge of the business to enrich themselves at the expense of the shareholders (Heath & Norman, 2004).

The collapse of the governance relationship in the Enron-era scandals reflected the failure of these companies and their shareholders to defend themselves against conflicts with agencies (Heath & Norman, 2004).

UK regulators, for example, adopted the agency view of corporate governance (McKnight & Weir, 2009) and took steps to monitor, control and sanction companies and company directors to maintain the confidence of the capital market. One such step involved the formation of various committees, each with the remit to improve corporate governance in UK listed companies. Since the initial Cadbury Code of 1992, the UK has periodically ordered reviews of the corporate governance of listed firms, each one resulting in additions to the previous set of recommendations. This eventually came to be known as the Combined Code on Corporate Governance (Dedman, 2016).

2.2.3 Stakeholder theory

Milton Friedman, an economist who posited the stakeholder theory in the early 20th century, suggests that a company's aim is to make money for stockholders, which means that stockholders are the one and only group of stakeholders that managers can consider when making a decision. Nonetheless, in recent times, some economists have continued to embrace the stakeholder theory as offering a range of possible economic advantages. Many businesses understand that economic health affects all stakeholders including owners, vendors, staff and consumers (Corfield, 1998). The stakeholder model understands the company as a private body responsible and accountable to a wider group of stakeholders (Wieland, 2005).

According to West (2006), the stakeholder model is focused on the company's view of a social organisation that has duty (and accountability) to a range of stakeholders, in its broadest context, including all those who influence or are affected by the business. This typically includes shareholders, vendors, consumers, workers, management, government and local communities. This view is supported by Heath and Norman (2004), who state that the governance stakeholder theory is concerned with how specific groups of stakeholders should exercise oversight and management control.

According to Corfield (1998), under stakeholder theory, directors take into account the company's best interests when discharging their duties. This binds them to consider the consequences of any action on all groups affected by their action, including shareholders, staff, vendors, clients, business creditors and community in which the company is located.

A range of stakeholders has been identified, namely, contractual stakeholders such as employees, customers, suppliers, bankers and creditors, and non-contractual stakeholders such as the media, special interest groups, local communities, society at large, professional bodies, the state and the government. It is, however, evident that certain stakeholders, besides shareholders, enjoy distinct prominence. It is especially local communities and society that are being singled out as prominent stakeholders and the social responsibility of companies towards society is consequently emphasised (Rossouw, 2005).

Two influential economists, the UK's Will Hutton and the USA's Margaret Blair, are ardent supporters of the stakeholder theory. Hutton sees this theory as the solution to massive injustice, underinvestment and a hollow-out manufacturing base that ultimately does little good to any sector of the economy. Blair believes that managing companies with the interests of all stakeholders in mind is in a country's long-term economic interest (Corfield, 1998). Corfield supports Hutton and Blair's views and argues that the age-old notion of ownership and control—where the corporation is an asset of the shareholders—should be discarded. Instead, the corporation should be treated as a governance system whose social function is to administer the wealth and investments made by all the stakeholders of the company (Corfield, 1998).

According to Blair, boards of directors should recognise that they represent all the stakeholders of a company, and not just shareholders. They should aim to optimise the business' wealth creation (Corfield, 1998). Heath and Norman (2004) concur, stating that in the stakeholder theory, shareholders are but one of several important stakeholder groups. Customers, suppliers, employees and local communities also have a stake in the firm's success or failure and are affected by it. The firm and its managers have special obligations to ensure that shareholders receive a fair return on their investment, but the firm also has special obligations to other stakeholders, which go above and beyond those required by law.

The implementation of corporate governance stakeholder theory and the consideration of a wider group's interests, other than just the shareholders, is in line with the rapidly evolving corporate world, including the increasing importance of environmental concerns and more demanding workers, societies and consumers. This means treating stakeholders equally and justly (Corfield, 1998).

Summative comment on theories of corporate governance

The shareholder theory deals with situations where one person—the principal—wants to induce another—the agent—to perform some task that is in the interest of the principal, but not necessarily that of the agent. Governance stakeholder theory is concerned with how specific stakeholder groups can exercise regulation and management power. This is important when considering the impact that any event or decision would have on all of the organisation's stakeholders.

Corporate governance is sometimes defined as being either Anglo-American or European. Typically, the Anglo-American approach tends toward the shareholder model, which is also a one-tiered board structure, while the European approach tends towards the stakeholder model, which is a two-tiered board structure (West, 2006; Maassen, 1999). The following section will provide an explanation on the one- and two-tiered board structures.

2.2.4 One-tiered and two-tiered board structures

Reed (2002) claims that developing countries implement corporate governance reforms in line with the Anglo-American (shareholder) approach, which he defines as having the following characteristics:

- a single-tier board structure that gives the shareholders' interests almost absolute primacy;
- dominant role of financial markets;
- a correspondingly weak financial position; and
- little to no labour policy concerning businesses cooperating with state agencies.

In general, Anglo-American countries such as the USA, the UK and Canada have adopted variants of the one-tier board model. In this model, executive directors and non-executive directors operate together in one organisational layer (the so-called one-tier board). Some one-tier boards are dominated by a majority of executive directors while others are composed of a majority of non-executive directors. In addition, one-tier boards can have a board leadership structure that separates the CEO and chair positions of the board. One-tier boards can also operate with a board leadership structure that combines the roles of the CEO and the chairman. This is called CEO-duality. One-tier boards also often use board committees such as audit, remuneration and nomination committees (Maassen, 1999; Bendixen & Thomas, 2000). King IV is an example of a one-tier board recommendation.

Continental European countries such as Germany, Finland and the Netherlands have adopted variants of the two-tier board model. This is also confirmed by Bendixen and Thomas (2000), who state that this structure is commonly found in Germany, France and the Netherlands and has been proposed as a model for boards in the EU. In this model, an additional organisational layer has been designed to separate the executive function of the board from its monitoring function. The oversight board (the upper layer) is entirely composed of non-executive supervisory directors who may represent labour, the government and/or institutional investors. The management board/executive committee (EXCO, which is the lower layer) is usually composed of executive managing directors. It is generally not accepted that directors combine the CEO and chairman roles in two-tier boards. Because the CEO has no seat on the oversight board, the board's leadership structure is formally independent from the executive function of the board. This is particularly the case in two-tier boards in the Netherlands and Germany. In variants of the two-tier board model in these countries, executive managing directors are not entitled to have a position on the oversight board of the corporation (Maassen, 1999).

Table 2.1 below illustrates the difference between the one-tier board model and the two-tier board model.

Table 2.1: Difference between the one-tier board model and the two-tier board model

One-Tier Board Model	**Two-Tier Board Model**
The Board of Directors	**The Oversight Board**

In charge of decision management and decision control.	In charge of decision control, oversight and governance.
	The Management Board/EXCO In charge of decision management on a day-to-day basis.

Source: Maassen (1999).

Corporate failures and company collapses, combined with deceptive financial reporting practices, have prompted innovations in corporate governance, giving rise to numerous corporate governance standards, which have been issued since 1992 (Marx, 2008). The corporate governance literature is strongly dominated by research on one-tier corporate boards in the USA and the UK. Second in prevalence, but much less available, are studies on corporate governance models in Germany and the Netherlands. With the exception of a few studies, comparative research on governance systems and board models in (continental) European countries is hardly existent (Charkham, 1994; Pic, 1997; Maassen, van den Bosch & Volberda, 2004). For this reason, the following section adds to the existing body of knowledge by discussing the development of corporate governance codes within the selected international countries, such as the UK, USA, Australia and the Netherlands. It then concludes with a detailed discussion of the corporate governance developments in South Africa.

Critical link to the empirical study:

The stakeholder theory emphasises the importance of all stakeholders. Auditing firms have an important responsibility towards the public interest. For this reason, it is extremely important that auditing firms adopt the stakeholder theory as their corporate governance model and more specifically, a two-tier board structure.

The empirical study aims to provide guidelines on corporate governance practices and oversight structures for auditing firms in South Africa (based on the stakeholder theory and a two-tiered board structure) with principles that are specifically relevant to auditing firms.

2.3 Introduction to corporate governance codes

Corporate governance is a new discipline that has grown out of deep-seated concerns stemming from spectacular and well-publicised corporate failures, which are also discussed in Chapter 3. This section in Chapter 2 aims to contribute to the body of knowledge by discussing the developments of corporate governance codes internationally and locally in South Africa. This section also discusses any corporate governance codes, acts or legislation that are applicable to auditing firms.

According to Gregory and Simms (1999) the modern trend of developing corporate governance in the USA was a response to problems in the corporate performance of leading companies, the perceived lack of effective board oversight that contributed to those performance problems and pressure for change from institutional investors. The corporate governance developments in the UK and USA proved to be influential sources for other guidelines and code efforts. The UK also influenced the development of the King Code in South Africa. This is confirmed by West (2006), who states that South African corporate law and corporate practice have been adopted mainly from the UK. The UK and USA also faced some of the most well-known corporate failures that led to the development of corporate governance codes. These corporate failures include Enron in the USA and Robert Maxwell in the UK (Clarke, 1993; Aziri, 2014). For these reasons, the UK and USA were selected for this study.

Australia is no different to the UK and USA and also faced some well-known corporate scandals. These include HIH Insurance, One.Tel, Ansett Australia and Harris Scarfe (Mirshekary et al., 2005). A corporate governance code was also developed after these scandals.

The Netherlands was selected because it adopted a different board model to the UK, USA and Australia. According to Bendixen and Thomas (2000), the Netherlands adopted a two-tier board model. Countries like the UK, USA, Australia and South African mostly have a one-tier board model.

As mentioned in Chapter 1, there is very little legislation, standards or codes that govern the corporate governance of auditing firms. In South Africa, the APA 26 of 2005 only provides information on the governance of the regulatory board, but no specific information on auditing firms and audit firm governance. The Brydon Report was issued in 2019 and provided recommendations on the improved quality and effectiveness for auditing in the UK. The Brydon Report also specifically proposes a set of principles, namely, the Principles of Corporate Auditing, which relate to governance. From the extensive literature review, it emerged that the UK is the only country with a corporate governance code specifically for auditing firms, namely, the Audit Firm Corporate Governance Code. Globally, there is the ISQC 1 and ISA 220 that provide limited information on audit quality and governance. The drafts for the International Standard on Quality Management (ISQM) 1 and ISQM 2 were released in 2019, but are not yet effective. For this reason, this study discusses the literature on ISQC 1 and ISA 220 only.

The following sections of the chapter discuss the corporate governance codes applicable in each country as stated above. Should there be a corporate governance code for auditing firms in a specific country, this code is also discussed under the relevant country's heading.

2.3.1 Corporate governance in the UK

2.3.1.1 Corporate governance codes applicable to all corporate entities

In the UK, corporate failures and scandals prompted the development of voluntary codes as well as some attempts at the legislated approach on corporate governance (Pandhu, n.d.). A series of sensational business scandals occurred in the UK in the late 1980s. There was particular public indignation at Robert Maxwell's plundering of pension funds, at the inability of auditors to reveal the Bank of Credit and Commerce International's imminent collapse and at the relatively high pay increases earned by senior executives. In response, the City of London formed a special committee to investigate the financial dimensions of corporate governance. This was the Cadbury Committee's Code of Best Practice. The Industrialist, Sir Adrian Cadbury, chaired this committee. The Cadbury Committee report, as it came to be known, created public awareness about the most effective means of regulating the actions of company managers and executives to ensure ethical behaviour. The 1992 Cadbury Report defines corporate governance as the systems that direct and control companies. The Cadbury Code proposed a greater presence on corporate boards for non-executive directors, numerous improvements in board procedures and a more active role for auditors (Boyd, 1996).

The Cadbury Committee released the first edition of the UK Corporate Governance Code, in 1992. It described corporate governance as the structure that guides and regulates businesses. Boards of directors are responsible for the management of their businesses. The position of the shareholders in governance is to appoint the directors and auditors and to ensure that there is an effective governance system in place. This remains valid today, but the world in which companies, their shareholders and wider stakeholders work, continues to evolve rapidly (FRC, 2019).

The next report was called the Myners Report which was produced by a committee chaired by Paul Myners in 1995. It concentrated on the relationships between companies and institutional investors. It recommended that when a company is performing badly, institutional investors should attempt to rectify the problem instead of selling their shares and turning their backs on the company. It argued for a legislated approach in dealing with corporate scandals as opposed to the voluntary codes (Pandhu, n.d.).

The next code was the Greenbury Report prepared by the Greenbury Committee. It was set up on the recommendation of the Cadbury Committee to review progress on corporate governance in the UK and state companies. Published in 1995, it focused mainly on directors' remuneration. This report was a direct response to the UK media onslaught on the 'fat cat' directors who over-remunerated themselves at the expense of shareholders, especially in newly privatised companies. This report recommended the establishment of remuneration committees and associated disclosures on director remuneration. It also recommended the crafting of sound remuneration policies and performance-based director service contracts (Pandhu, n.d.).

The next report was the Hampel Report which was drafted in 1995 by Sir Ronald Hampel. Its sole task was to review the recommendations of the Cadbury and Greenbury Committee Reports. The report was finally published in 1998 and covered the following corporate governance issues: the ideal composition of the board and the role of directors, directors' remuneration, the role of shareholders, particularly institutional investors, communication between the company and its shareholders, financial reports, auditing and financial statements (Pandhu, n.d.).

In 2003, the Hicks and Smith Report on corporate governance was published. It articulated the roles and responsibilities of non-executive directors and issued guidelines on the roles and responsibilities of audit committees (Pandhu, n.d.).

Early in 2009 Sir John Walker prepared the latest code on corporate governance for the UK, giving rise to the Combined Code. The Combined Code was born out of the need to combine all efforts on corporate governance in the UK. It was important that the UK stock exchanges required listed companies to disclose in their annual report the extent of their compliance with the Combined Code. The Combined Code provided for periodic reviews of its terms, to take into account changes in corporate governance in the UK (Pandhu, n.d.).

A variety of factors guided the review of corporate governance during 2017–2018 which contributed to the 2018 Code. These included a continuing lack of confidence in business, high-profile corporate failures, lingering concerns that businesses had given little thought to long-term sustainability, and more generally, the impact that businesses have on wider society (FRC, 2020). Continued corporate failures also raised concerns about the effectiveness of the board's long-term sustainability in considering and reporting on risks. Through the review by the FRC it became clear that many businesses only concentrated on ensuring strict compliance with regulations and that this strategy provided little insight into governance practices. Most companies declared themselves fully compliant with the Code; however, there was a lack of information on the results of governance policies and practices in many annual reports, including any areas for future improvement (FRC, 2020).

The 2018 Code reaffirms the value of implementing the Principles in a way that shareholders can determine. It is much more important to apply the concepts efficiently than to use a 'tick box' approach. It involves showing the actions that an organisation has taken and how these relate to its strategy and intent. This is supported by the language used in the 2018 Code. There are many cases in which companies are asked to explain the impact of their actions, such as stakeholder and employee engagement and progress against the outcomes of diversity (FRC, 2020).

The Code has been updated and extended over the years to take into account rising demands on the UK's corporate governance system. Theory of mutual accountability within a unitary board has been a success and has played a critical role in achieving good governance standards and promoting long-term investment alongside investor stewardship activities. Nevertheless, the debate on the complexity and scope of the system has escalated as a result of financial crises and high-profile cases of insufficient governance and corruption, leading to disappointing outcomes for a wide variety of stakeholders (FRC, 2019).

The essence of the new Code is a revised collection of principles that stresses the importance of corporate governance to sustainable long-term success. By adopting the Principles, observing the more comprehensive guidelines and using the related guidance, businesses are able to show in their reporting how the company's governance leads to its sustainable long-term performance and meets wider objectives (FRC, 2019). Achieving this depends crucially on the way boards and companies apply the spirit of the Principles. The Code does not set out a rigid set of rules; instead it offers flexibility through the application of Principles and through 'comply or explain' provisions and supporting guidance. It is the responsibility of boards to use this flexibility wisely, and of investors and their advisors to assess differing company approaches thoughtfully (FRC, 2019).

The 2018 Code focuses on applying the Principles. The listing rules require businesses to state how they have applied the Principles, in a manner that will allow shareholders to determine how the Principles were implemented. It is critical for investors to be able to assess the governance approach. Reporting covers the implementation of the Principles in the sense of the company's specific circumstances and how the board set the mission and strategy of the company, reached targets and achieved results through its decisions (FRC, 2019).

When discussing the implementation of the Principles and avoiding 'boilerplate' reporting, it is necessary to report meaningfully. The emphasis would be on how the Principles were applied, articulating what action was taken and the consequences that resulted. High-quality reporting must involve signposting and cross-referencing to all sections of the annual report, explaining the implementation of the principles. This helps investors to evaluate business activities (FRC, 2019). Corporate governance reporting should also relate coherently to other parts of the annual report, particularly the Strategic Report and other complementary information, so that shareholders can effectively assess the quality of the company's governance arrangements and the board's activities and contributions FRC, 2019).

The 2018 Code is applicable to all companies with a premium listing, whether incorporated in the UK or elsewhere. The new Code applies to accounting periods beginning on or after 1 January 2019 (FRC, 2019).

The Principles of the 2018 Code include the following:

i. Board leadership and company purpose;
ii. Division of responsibilities;
iii. Composition, succession and evaluation;
iv. Audit, risk and internal control; and
v. Remuneration (FRC, 2019).

More details about these Principles can be found in Annexure B.

Summative comment on corporate governance codes in the UK

Corporate failures in the 1980s led to the development of the Cadbury Code. Many more codes followed, such as the Myners Report, the Greenbury Report, the Hampel Report, the Hicks and The Smith Report and finally in 2009, the Combined Report, which was a combination of these reports. The Combined Report was reviewed several times, based on changes in corporate governance. The 2018 Code is applied in the UK, namely, the 2018 Combined Code. This Code consists of five principles, namely, (1) Board leadership and company purpose, (2) Division of responsibilities, (3) Composition, succession and evaluation, (4) Audit, risk and internal control and (5) Remuneration. The Code is not a set of rules, but rather principles that should be applied through a 'comply or explain' method. The Code is applicable to all companies with a premium listing and applied to accounting periods beginning on or after 1 January 2019. The corporate governance with respect of auditing firms are not specifically addressed.

2.3.1.2 Corporate governance codes applicable to auditing firms in the UK

As stated previously, the UK is the only country in the world that has a corporate governance code specifically for auditing firms. The Brydon Report was also released in 2019 in the UK, addressing some very important principles regarding auditing firms. Below is a detailed explanation of the Audit Firm Governance Code and some information on the Brydon Report which is applicable to this study.

2.3.1.2.1 The Brydon Report

As far as auditing companies are concerned, the Brydon Report was released in 2019. It includes a large number of recommendations that can be taken together to promote improved audit efficiency and effectiveness in the UK. The recommendations not only relate to auditors' work, but also to the role of other individuals' work in relation to the audit. There have been extensive discussions of the business framework with reference to audit as well as independence matters (Brydon, 2019).

The Brydon Report recommends a set of standards, referred to as the Corporate Auditing Standards. These seek to accord more importance to auditor behaviours set out in existing standards and codes, while incorporating additional concepts regarding transparency, freedom, challenge and the public interest. These standards would provide an opportunity to provide more detailed audits if successfully enforced and applied. The Brydon Report also provides recommendations for greater disclosure to help create trust in the corporate auditing profession (Brydon, 2019).

The principles of Corporate Auditing are to fulfil the purpose of auditing. These principles include the following:

- Auditors act with integrity, fulfilling their responsibilities with honesty, fairness, candour, courage and confidentiality;
- Auditors are appropriately qualified and exercise professional judgment and appropriate scepticism or suspicion throughout their work;
- Auditors act in the public interest and have regard for the interests of the users of their report beyond solely those of shareholders;
- Auditors maintain independence from the entity and its officers on whom they are engaged to report;
- Auditors are objective and provide findings and opinions unaffected by bias, prejudice, compromise and personal or corporate conflicts of interest;
- Auditors work to verify and encourage openness and honesty in financial and other company reporting;
- Auditors ask the directors to report any material information that may legitimately be disclosed to assist users in understanding the audit report and, if necessary, disclose it themselves;
- Auditors provide appropriate challenges to management, assessing critically information and explanations received for signs of over-optimism, judgmental bias or possible fraud;
- Auditors' reports contain clear findings and expressions of opinion setting out all information necessary for a proper understanding of the opinion and its basis; and
- Auditors' reports transparently reflect any differences of view with management and how they were resolved (Brydon, 2019).

According to Brydon (2019), these principles should provide an overarching structure for auditors' conduct beyond that which strictly follows norms and law. To ensure that the Corporate Auditing Principles are used as a living document, Brydon (2019) advises that each audit report include a declaration that the auditor has acted diligently, in compliance with the Corporate Auditing Principles in performing the audit.

The core focus, according to Brydon (2019), should be on the ethics of the profession. He argues that understanding the law and regulations is not the only response to ethical problems. Of course, the rule of law is important, but ethics is motivated by something more, and can affect conduct that goes beyond compliance with the law. Indeed, an ethical culture in auditing firms can, and should, exist even without direct regulatory interference.

From time to time the FRC has judged the actions of auditors against the expectations reasonably expected of a member. According to Brydon (2019), these judgments would be stronger if the Corporate Auditing Standards, as outlined here, were to be applied specifically to the auditor.

Brydon (2019) also emphasises the importance of acting in the public interest. According to Brydon (2019), auditors cannot act alone in the public interest; they need directors to do so too. This statement supports why this study is so important and why auditing firms should be governed correctly. It is clearly all about the tone at the top. The Brydon Report, like most other acts, reports and codes, focuses more on the governance structures of the individual auditor and auditor quality and not specifically on the governance and leadership of the auditing firm.

2.3.1.2.2 The Audit Firm Governance Code of the FRC

As mentioned in section 1.1, the FRC implemented the Audit Firm Governance Code in the UK in 2010, specifically for auditing firms.

The role of the FRC is to lead the development of auditing practice in the UK and establish high standards for auditing, meet the developing needs of users of financial information and ensure public confidence in the auditing process. To achieve these objectives, the FRC issues ISAs, which are mandatory practice notes that indicate good practice, and bulletins, which comment on items of current interest (Millichamp & Taylor, 2018).

Audit is a legislative role in which public interest is substantial. The UK Audit Firm Governance Code is intended to increase trust and confidence in the value of audit among the public and particularly investors. The Code refers to organisations that audit 20 or more of the listed entities (FRC, 2016).

The Code's aim is to provide a benchmark of corporate governance practice that can be disclosed to companies auditing listed firms. Its key objectives are to:

- Improve the standard of audits;
- Help the firm to secure its reputation more broadly, including its non-audit undertakings; and
- Reduce the probability of business collapses which will be of systemic importance in relation to the largest companies.

The Code is designed primarily to support investors. There is also interest from other stakeholders, including:

- Directors, in particular members of the audit committee, with responsibility for nominating auditors;
- Compliance audits; and
- Review partners and staff (FRC, 2016).

The Institute of Chartered Accountants in England and Wales (ICAEW) founded an independent working group in 2007 under the chairmanship of Norman Murray (then chairman of Cairn Energy Plc) to establish the Audit Firm Governance Code, at the invitation of the FRC. In January 2010, the Audit Firm Governance Code was jointly released by ICAEW and FRC. It contained 20 concepts and 31 rules and was 'comply or explain' based. This applied to companies that audited 20 or more of listed firms. This Code implemented two new definitions as well as codifying current standards and practice:

- Nomination of INEDs within corporate governance structures; and
- Dialogue between the listed companies and investors (FRC, 2016).

The FRC reviewed the application of the Code during 2014–2015. The analysis found that organisations within its scope (and at least one outside of it) had implemented the Code. The Code had been applied in different ways by organisations, with a specific variation in the role of INEDs within governance systems. Within this area the FRC does not wish to recommend a uniform method. Nonetheless, by encouraging audit efficiency, companies can publicly report on why they have followed a specific approach and whether that approach supports the public interest. This version of the Code was released in July 2016 and applies to financial years commencing on or after 1 September 2016 (FRC, 2016).

The review of the Code by the FRC also brought up a number of other issues:

- The Code itself is barely noticeable;
- Investors are not aware of the position played by INEDs and have doubts about their independence; and
- Investor dialogue has not functioned as well as expected. Corporate governance code elements may be usefully integrated into the Code (FRC, 2016).

Following the review, the FRC made a range of changes, in particular to help foster audit corporate governance, to improve transparency and to incorporate some additional provisions from the Code of Corporate Governance. The standards remain the same (FRC, 2016).

As stated in Chapter 1, transparency plays a crucial role in corporate governance. Through law, all entities that audit listed companies are required to create annual disclosure reports that include, inter alia, details on the application of the Code within that entity. These reports, however, are not widely read and have been identified as limited interest enforcement documents. In addition to providing stakeholder information, reporting promotes transparency and helps to ensure that leadership reflects on the primary governance and performance concerns it addresses (FRC, 2016).

The FRC believes companies should review their reports on transparency to provide information that is more applicable to investors, regulators and other stakeholders. In particular, companies applying the Code should ensure that their reports are fair, reasonable and comprehensible, as specified by the Audit Firm Governance Code. These reports should include the following aspects:

- Information on the work of the board of directors and the INEDs, including results against any of the members;
- New key performance indicators;
- A separate INED and/or Public Interest Committee report; some organisations are already doing this. This report should include an explanation of how, over the reporting period, the INED or the public interest committee in particular oversaw the UK audit practice and, more generally, the wider UK business;
- Information on what the board and the INEDs have done to ensure that there is a positive atmosphere in the organisation;
- An explanation of why the organisation has chosen to place its INEDs in the way it has and how it believes this serves the public interest by helping to improve the consistency of the audit;
- A description of how the board and the INEDs worked throughout the year to fulfil the function of the Code; and
- Information of any provisions of the UK Corporate Governance Code which, in addition to those already in the Code, the organisation has incorporated into its own governance frameworks, and if there are any other provisions which it may implement in the future (FRC, 2016).

The principles of this Code include:

- Leadership;
- Values;
- Independent Non-Executive Directors;
- Operations;
- Reporting;
- Dialogue.

Detailed information on the above principles can be found in Annexure C.

The FRC also provided a checklist in which it determines which principles contained in the UK Corporate Governance Code (as discussed in 2.3.1.1.) should be implemented by auditing firms.

This checklist, which can be found in Annexure D, is similar to the aim of the present study. This study seeks to provide guidelines on corporate governance practices and oversight structures for auditing firms in South Africa, based on King IV and guided by the UK Audit Firm Governance Code. These guidelines would be applicable to auditing firms in South Africa and could be included as a sector supplement to King IV. This checklist in Annexure D forms a key component of the empirical research in this study (FRC, 2016).

Summative comment on corporate governance codes in the UK

The Brydon Report was released in 2019, specifically providing principles to promote improved audit efficiency and effectiveness in the UK. The Brydon Report focuses more on the governance of the individual auditor and auditor quality, and not specifically on the governance and leadership of the auditing firm. In January 2010, the Audit Firm Governance Code was jointly released by ICAEW and FRC. It contained 20 concepts and 31 rules and was 'comply or explain' based. This Code applied to auditing firms which audited 20 or more of the listed firms. The FRC reviewed the application of the Code during 2014–2015. Following the review, the FRC made a range of changes, in particular to help foster audit corporate governance, to improve transparency and to incorporate some additional provisions from the Code of Corporate Governance. The fundamentals remain unchanged. All companies that audit listed companies are required to produce annual transparency reports by regulation. The Principles of this code include (1) Leadership, (2) Values, (3) Independent Non-Executives, (4) Operations, (5) Reporting, (6) Dialogue. The FRC provided a checklist that sets out which principles contained in the UK Corporate Governance Code should be implemented by auditing firms. From the checklist (see Annexure D) it is clear that Chapters 1 to 3 of the UK Corporate Governance Code can be applied to auditing firms.

2.3.2 Corporate governance in the USA

In the USA, no discernible interest existed in corporate governance before the 1990s Act (Marx, 2008). The Sarbanes-Oxley Act (SOX) (Pub.L. 107-204, 116 Stat. 745) enacted on 30 July 30 2002) marked a significant milestone for corporate governance in the USA. The Act, which was the legislative response to a series of high-profile financial scandals, was intended to rebuild investors' confidence in the capital markets (Engel, Hayes & Wang, 2007). Marx (2008) supports this statement, stating that the collapse of Enron, Arthur Anderson, World.Com and others from the late 2001, generated interest in corporate governance. As a result, a series of regulations and statutory provisions was enacted in 2002 through the well-known SOX Act (Marx, 2008). Murdock and Murdock, (2018) reiterated this, stating that the bill was enacted as a reaction to a number of major corporate and accounting scandals including those affecting Enron, Tyco International and WorldCom. These scandals, which cost investors billions of dollars when the share prices of affected companies collapsed, shook the public's confidence in the nation's securities markets. The USA approached the problem of corporate scandals by legislating corporate governance as opposed to opting for a voluntary code (Pandhu, n.d.).

The SOX Act is also known as the 'Public Company Accounting Reform and Investor Protection Act' (in the Senate), the 'Corporate and Auditing Accountability and Responsibility Act' (in the House) and is commonly called the Sarbanes Oxley, Sarbox or SOX. This federal law set new or enhanced standards for all USA public company boards, management and public accounting firms. It is named after the sponsors, Senator Paul Sarbanes (D-MD) and Representative Michael G. Oxley (R-OH) (Murdock & Murdock, 2018).

The SOX of 2002 is mandatory for all organisations, large and small (SOX, 2002). It does not apply to privately held companies (Murdock & Murdock, 2018). The legislation introduced major changes to the regulation of financial practice and corporate governance, with a number of deadlines for compliance (SOX, 2002).

According to Uzun et al. (2004), the passage of the SOX of 2002 was widely regarded as the most extensive USA federal law related to corporate governance since the implementation of the federal securities laws in 1933 and 1934. Another important response was the requirement that companies whose stock is traded on the NYSE or listed on Nasdaq meet various corporate governance provisions. The SOX of 2002 and NYSE and Nasdaq proposals impose several governance provisions on publicly traded companies in the USA and a significant stipulation was improved oversight by the company's independent directors (Uzun et al., 2004).

Over the past 12 years, more than half of the states that form the USA have adopted legislation for the group of stakeholders or non-shareholder. These statutes propose a different model of corporate governance to that traditionally used by American corporations, according to which directors act to maximise shareholder profits for the interests of the shareholders. These statutes of stakeholders, or statutes of non-shareholder interests, met with some opposition from the legal community and were reduced in many cases to being used as a pure anti-takeover tool. The statutes were used primarily in the USA to defend hostile takeovers that were viewed as contrary to public welfare (Corfield, 1998).

The Act makes numerous provisions in areas ranging from additional corporate board responsibilities to criminal penalties, and requires the SEC to implement rulings on requirements to comply with the new law. Harvey Pitt, the 26th chairman of the SEC, led the SEC in the adoption of numerous rules to implement the SOX Act. It created a new, quasi-public agency, the Public Company Accounting Oversight Board (PCAOB), charged with overseeing, regulating, inspecting and disciplining accounting firms in their roles as auditors of public companies. The Act also covers issues such as auditor independence, corporate governance, internal control assessment and enhanced financial disclosure. The Act was approved by the House by a vote of 421 in favour, 3 opposed and 8 abstaining and by the Senate with a vote of 99 in favour, 1 abstaining. President George W. Bush signed it into law, stating that it included the most far-reaching reforms of American business practices since the time of Franklin D. Roosevelt (Murdock & Murdock, 2018).

Debate continues over the perceived benefits and costs of SOX. Supporters contend the legislation was necessary and has played a useful role in restoring public confidence in the nation's capital markets by, among others, strengthening corporate accounting controls. Opponents of the bill claim it has reduced America's international competitive edge against foreign financial service providers, saying SOX has introduced an overly complex regulatory environment into USA financial markets. Proponents of the measure view SOX as a 'godsend' for improving the confidence of fund managers and other investors with regard to the veracity of corporate financial statements (Murdock & Murdock, 2018).

SOX contains 11 titles which describe specific mandates and requirements for financial reporting. Each title consists of several sections (Murdock & Murdock, 2018). The 11 titles include the following: (1) PCAOB, (2) Auditor Independence, (3) Corporate Responsibility, (4) Enhanced Financial Disclosures, (5) Analyst Conflict Interest, (6) Commission Resources and Authority, (7) Studies and Reports, (8) Corporate and Criminal Fraud Accountability, (9) White Collar Crime Penalty Enhancement, (10) Corporate Tax Returns and (11) Corporate Fraud Accountability. A detailed review of the 11 titles can be found in Annexure E.

From the literature review, no specific corporate governance code for auditing firms in the USA could be found.

Summative comment on corporate governance codes in the USA

The SOX was the response to high-profile scandals in the USA and was intended to rebuild the confidence of investors in capital markets. The main contributors to SOX were Senator Paul Sarbanes and Representative Michael Oxley, after whom the Act is named. SOX is regarded as one of the most extensive federal laws, as it is not a voluntary code, but rather legislation. SOX is mandatory for all organisations, large and small. The Act contains 11 titles include the following: (1) PCAOB, (2) Auditor Independence, (3) Corporate Responsibility, (4) Enhanced Financial Disclosures, (5) Analyst Conflict Interest, (6) Commission Resources and Authority, (7) Studies and Reports, (8) Corporate and Criminal Fraud Accountability, (9) White Collar Crime Penalty Enhancement, (10) Corporate Tax Returns and (11) Corporate Fraud Accountability.

2.3.3 Corporate governance in Australia

The Corporate Governance Council of the ASX released the Principles of Good Corporate Governance and Best Practice Recommendations in 2003. It outlined 10 specific principles to create an effective governance framework for corporations. The recommendations, known as the Corporate Governance Guidelines (ASX, 2005), are not compulsory, but ASX Listing Rule 4.10.3 specifies that each listed company must disclose in its annual report the degree to which it complies with the recommendations and include any reason for failure to comply (Christensen et al., 2010).

According to Alan Cameron, Chair of the ASX Corporate Governance Council (2014), the ASX Corporate Governance Council Principles and Recommendations were substantially re-written and a second edition was released in 2007. This version included new recommendations on diversity. The composition of the remuneration committee was added in 2010 (ASX Corporate Governance

Council, 2005). This is supported by Marx (2008), who explains that the 2001 Ramsay Report and the 2003 Owen Report recommended significant external audit changes as well as significant input into the process of CLERP 9. The ASX Corporate Governance Committee released principles on corporate governance and guidelines to guide listed companies (Marx 2008).

Since the release of the second edition in 2007, there has been considerable focus across the world on corporate governance practices in light of the events leading up to and during the global financial crisis. In response, a number of jurisdictions have adopted new legislation regulating corporate behaviour and/or upgraded their corporate governance codes (ASX Corporate Governance Council, 2005).

Following a comprehensive review from 2012 to 2013, the 21 members of the ASX Corporate Governance Council agreed that it was an appropriate time to issue a third edition of the Principles and Recommendations. The changes in the third edition reflect global developments in corporate governance since the second edition was published.

In 2017, the ASX Corporate Governance Council agreed that it was an appropriate time to commence work on a fourth edition of the Principles and Recommendations to address emerging issues linked to culture, values and trust, fuelled by recent examples of misconduct by some listed entities, which had fallen short of community standards and expectations. The fourth edition came into force for the financial years commencing on or after 1 January 2020 (ASX Corporate Governance Council, 2019).

These Principles and Recommendations set out recommended corporate governance practices for entities listed on the ASX that, in the Council's view, are likely to achieve good governance outcomes and meet the reasonable expectations of most investors in most situations. The Council recognises, however, that different entities may legitimately adopt different governance practices, based on a range of factors, including their size, complexity, history and corporate culture. For that reason, the Principles and Recommendations are not mandatory and do not seek to prescribe the corporate governance practices that a listed entity should adopt (ASX Corporate Governance Council, 2019).

The Principles and Recommendations promote eight central principles:

i. Laying solid foundations for management and oversight;
ii. Structuring the board to be effective and add value;
iii. Instilling a culture of acting lawfully, ethically and responsibly;
iv. Safeguarding the integrity of corporate reports;
v. Making timely and balanced disclosure;
vi. Respecting the rights of security holders;
vii. Recognising and managing risk; and
viii. Remunerating fairly and responsibly (ASX Corporate Governance Council, 2019).

A detailed description of the principles above can be found in Annexure F.

In Australia there is no specific corporate governance code for auditing firms.

Summative comment on corporate governance codes in Australia

In 2003, the ASX released the Ramsay Report of 2001, which contained the Principles of Good Corporate Governance and Best Practice Recommendations. A second edition, namely the Owen Report, was released in 2007, with some new recommendations added in 2010. From 2012 to 2013, there was a comprehensive review and a third report was issued. In 2017, there was another review and the fourth edition was released. This Report, which is applicable to all listed entities, consists of eight non-mandatory Principles: (1) laying solid foundations for management and oversight, (2) structuring the board to be effective and add value, (3) instilling a culture of acting lawfully, ethically and responsibly, (4) safeguarding the integrity of corporate reports, (5) making timely and balanced disclosure, (6) respecting the rights of security holders, (7) recognising and managing risk, and (8) remunerating fairly and responsibly. This fourth edition of the Report is applicable to accounting periods from 1 January 2020. The corporate governance with respect of auditing firms are not specifically addressed by the Australians.

2.3.4 Corporate governance in the Netherlands

The corporate governance system in the Netherlands has witnessed important changes over the last decade. Following a very public debate about the maintenance of the wide arsenal of defensive measures against takeovers in the first half of the 1990s, a first attempt was made to produce corporate governance recommendations for listed companies (van Bekkum, Hijink, Schouten & Winter, 2010).

According to de Jong, DeJong, Mertens and Wesley (2005), the Committee on Corporate Governance, also known as the Peters Committee, launched the debate on corporate governance in 1997. The Committee issued 40 recommendations designed to increase management efficiency, oversight and accountability to Dutch company investors. According to van Bekkum et al. (2010), 40 Peters Committee guidelines were released in 1997, causing a general understanding of corporate governance (van Bekkum et al., 2010). As such, the Peters Committee's recommendations may be seen as the Netherlands' first corporate governance code (Akkermans, van Ees, Hermes, Hooghiemstra, van der Laan, Postma & van Witteloostuijn, 2007).

The discussions on corporate governance took place against the background of the Dutch corporate law system which imposed a stakeholder rather than a shareholder orientation of the company's executive and oversight boards (also often referred to as supervisory boards). In general, Dutch corporate law also provides for a broad variety of measures that can be used not only to protect companies from hostile takeovers, but also to substantially minimise the participation of shareholders in corporate matters under normal circumstances, including non-voting depositary receipts for shares, priority shares with special control rights and formal delegation of authority to the executive board (van Bekkum et al., 2010).

The Dutch code of corporate governance, also known as the Tabaksblat Code, was released in December 2003 and came into effect on 1 January 2004. As of that date, listed companies were required to present a separate chapter in their annual reports on corporate governance (Akkermans et al., 2007). Established at the initiative of the Minister of Finance and the Minister of Economic Affairs, the Tabaksblat Committee included representatives of shareholders, listed firms, the stock exchange (Euronext Amsterdam) and institutional investors. Chaired by Mr Tabaksblat, its key mission was to draft a new code of corporate governance in the Netherlands. By doing so, it had to take into account international developments and the Peters Committee's guidelines, focus on listed companies and formulate a principles-based code. The Committee was also required to accept current corporate law as a matter of fact, while it was free to make proposals to reform legislation. The Committee published its draft code in July 2003 and invited stakeholders to come forward with suggestions for change. More than 250 individuals and organisations responded. The final edition of the Tabaksblat Code was published in December 2003. The Code contains 21 corporate governance principles which represent the most recent general views on good corporate governance (Corporate Governance Committee, 2003; Akkermans et al., 2007).

These principles were developed in the form of specific provisions relating to best practice. According to the Committee, these regulations provided a set of criteria for the actions of members and shareholders of the management board and the oversight board (Corporate Governance Committee, 2003). The Tabaksblat Code presents principles and best practice provisions in five areas: (1) compliance with and enforcement of the Code, (2) the management board, (3) the supervisory board (referred to in this study as the oversight board), (4) the shareholders and general meeting of shareholders, and (5) financial reporting.

The Tabaksblat Code refers to all companies listed on the Dutch stock exchange as well as to foreign companies with a Dutch statutory residence. In addition, and similar to many other national corporate governance codes, the Tabaksblat Code is based on the principle of 'comply or explain'. As of the fiscal year 2004, listed companies were legally required to show to what degree the organisation complied with the best practice provisions of the Tabaksblat Code, on the basis of the conformity or clarification principle (Akkermans et al., 2007). This is confirmed by van Bekkum et al. (2010), who indicate that the 2003 Corporate Governance Code was a 'comply or explain' code made mandatory by a Royal Decree as of 2004 for share-listed Dutch companies.

The main objectives of the Dutch Corporate Governance Code are to increase transparency and accountability and to improve the quality and integrity of management and oversight boards. More broadly, the Dutch code seeks to improve corporate management behaviour (Akkermans et al., 2007).

Corporate governance scandals in 2003 spurred the adoption of the Code. The most notable of these scandals was linked to the deceptive financial statements released by Royal Dutch Ahold and Royal Dutch Shell's oil reserves claims. The Corporate Governance Code includes concepts that are widely agreed and provide comprehensive guidelines on best practice of the Executive Board, the Supervisory Board (Oversight Board for the purposes of this study) and the General Meeting (call to institutional investors) (van Bekkum et al., 2010).

The two-tiered board structure, consisting of a management board and an oversight board, is primarily implemented by Dutch listed companies. The Dutch board structure can be traced back to 1602, to the world's first listed company, the VOC, or *Vereenigde Oostindische Compagnie*, which stands for Dutch East India Company. The VOC adopted a form of oversight board in 1623 following shareholder pressure to strengthen the governance of the firm. For companies regulated by the structure system, the two-tier model is required, in which case the workers have the right, through the works council, to appoint candidates for one-third of the oversight board members. Most large, listed companies are excluded from the structure rule, which may result in them opting for a one-tier board. Among the larger listed firms, only one has formally accepted the one-tier board, namely Unilever N.V. (van Bekkum et al., 2010).

The oversight committee for Corporate Governance Law, otherwise known as the Frijns Committee, amended the December 2003 Dutch Corporate Governance Code. The revised Code substituted the 2003 Code (Corporate Governance Code Monitoring Committee, 2008). The updated Code contained principles and best practice provisions which regulated relations between the management board, the oversight board and the shareholders (i.e. the general meeting of shareholders). The interests of the employees were taken into account when the interests of all stakeholders were weighed in connection with compliance with the Code (Corporate Governance Code Monitoring Committee, 2008).

The principles were regarded as reflecting the general views on corporate governance, and enjoyed wide support. The principles were elaborated in the form of specific best practice provisions, which created a set of standards governing the conduct of management board members, oversight board members and shareholders. They reflected national and international best practices and were regarded as elaborating the general principles of corporate governance. Listed companies departed from the best practice provisions; however, departures could be justified in certain circumstances (Corporate Governance Code Monitoring Committee, 2008).

The new Code was based on the principle that a company is a long-term relationship between the different parties involved in the company. The stakeholders are groups and individuals (i.e. employees, shareholders, lenders, suppliers, customers, the public and civil society), that influence or are influenced directly or indirectly by the achievement of the company's goals. The management board/EXCO and the oversight board have ultimate responsibility for balancing these concerns, usually with a view to ensuring the stability of the business, as the company seeks to build long-term value for shareholders (Corporate Governance Code Monitoring Committee, 2008).

The management board/EXCO and the oversight board should take account of the interests of the various stakeholders, including CSR issues that are relevant to the enterprise. If stakeholders are to cooperate within and with the company, it is essential for them to be confident that their interests are represented. Good stewardship, which includes integrity and transparency of the management board's actions, as well as effective supervision of their actions and accountability for such supervision, are essential conditions for stakeholder confidence in management and supervision.

These are the two pillars on which corporate governance is founded and which are the basis of this Code (Corporate Governance Code Monitoring Committee, 2008).

The amended Code came into force with effect from the financial year starting on or after 1 January 2009. The Committee recommended that listed companies include a chapter in their annual report on the broad outline of their corporate governance structure and compliance with the amended Code. Companies were to present this chapter at the general meeting in 2010 for discussion as a separate agenda item (Corporate Governance Code Monitoring Committee, 2008). The Code was divided into five chapters: (1) compliance with and enforcement of the Code, (2) the management board, (3) the supervisory board, (4) the shareholders and the general meeting of shareholders, and (5) the audit of the financial reporting and the position of the internal audit function and the external auditor. All these chapters contained principles and best practice provisions for listed companies.

In December 2016, the Corporate Governance Code Monitoring Committee announced in a press release that the Dutch Corporate Governance Code would be adapted. Ongoing developments, the spirit of the times and overlaps with legislation were reasons for the proposed amendment. This new Code replaced the 2008 Code in 2016 (Corporate Governance Code Monitoring Committee, 2016).

According to the Oversight Committee for the Corporate Governance Code (2016), the most important changes in the amended Code compared with 2008 version were as follows:

- Formulating and executing long-term value creation views allows the management board/EXCO members and members of the oversight board to behave in a sustainable manner by making deliberate decisions about the long-term sustainability of the plan being pursued;
- The incorporation of culture into the Code requires members of the management board/EXCO and the oversight board to create an environment that facilitates the desired actions within the company and ensures the dignity of employees. In practical terms, this means that principles must be formulated which fit into the company’s views. The management board/EXCO is required to promote behaviour that is consistent with these values and to actively propagate these values by leading by example;

- An important part of the Code is provisions which promote insight into the quality of risk management systems;
- In order to improve the internal audit process, the oversight board should be more closely involved in the hiring, assessment and potential dismissal of the lead internal auditor as part of the risk management program;
- New emphasis was placed on the composition of the management board/EXCO and the oversight board, contributing to controls and balances, effective corporate governance and independent supervision. Diversity in the oversight board and the management board/EXCO encourages judicious decision-making in terms of male-to-female ratios, skills, competencies and history. More clarity is required about measure, goals and steps that are taken;
- The appointment period for members of the oversight board was changed;
- Another improvement was that the Code prioritised the EXCO;
- Compared with the 2008 Code, the number of provisions on the subject of remuneration was reduced and the requirements were less detailed;
- The Code applies to companies with a two-tier board structure but also to companies with a one-tier board structure;
- Minimal amendments were made to the General Assembly.

According to the Corporate Governance Code Monitoring Committee (2016) the principles of the 2016 Code can be divided into five chapters, with each chapter containing several principles. The five chapters are as follows: (1) long-term value creation, (2) effective management and supervision, (3) remuneration, (4) the general meeting and (5) one-tier governance structure. These principles are discussed in detail in Annexure G.

In the Netherlands, there is no specific corporate governance code for auditing firms. According to KPMG the Netherlands (2018) Integrated Report, the audit firm applies the two-tier board structure and have an independent supervisory board. This too is the case for PwC, EY and Deloitte in the Netherlands. These auditing firms have independence on their boards through the supervisory committee, as specified in the Dutch Corporate Governance Code.

Summative comment on corporate governance codes in the Netherlands

In 1997 the Peters Committee issued 40 recommendations to investors of Dutch companies that triggered awareness of corporate governance. This came to be known as the first corporate governance code in the Netherlands. After corporate governance scandals in 2003, the Dutch Corporate Governance Code, also known as the Tabaksblat Code, was published in 2003 by the Tabaksblat Committee and became effective on 1 January 2004. Companies were expected to present a corporate governance chapter in their annual reports. A stakeholder approach was followed, which consisted of the two-tier board structure. The Code was reviewed in 2008 by the Frijns Committee and the amended Code came into force on or after 1 January 2009. In December 2016, the Code was adapted again. The 2016 Code consists of five chapters that contain 24 principles. The five chapters are as follows: (1) long-term value creation, (2) effective management and supervision, (3) remuneration, (4) the general meeting and (5) one-tier governance structure. The Code applies to all listed companies on a 'comply or explain' basis. The corporate governance with respect of auditing firms are not specifically addressed by the Dutch.

2.4 Corporate governance in South Africa

2.4.1 Corporate governance applicable to all entities in South Africa

Between 1961 and 1994, South Africa was virtually isolated from the global economy (Mathieson, Richards & Sharma, 1998; Sethi & Williams, 2000). Because of the country's oppressive political environment, the United Nations excluded South Africa from participating in international organisations and imposed economic and trade sanctions against the country, effectively stifling its economic growth. These tariffs and political isolation also protected South African firms from foreign competition, as financial sanctions kept international institutions out of the domestic market and domestic firms out of international capital markets (Malherbe & Segal, 2001). Consequently, corporate practices and national laws and regulations fell far behind international norms and, by the late 1980s, many of South Africa's corporations were unfocused entities run by complacent and entrenched managers (Vaughn & Ryan, 2006).

In 1994, retired judge, Mervyn King was appointed to form a commission to establish a code on governance in South Africa. The South African document on corporate governance is the King Report on Corporate Governance that was published in 1994. The Report was commissioned by the IoDSA. This initiative was amongst others supported by the South African Chamber of Business (SACOB), the Institute of Chartered Secretaries and Administrators (ICSA), the South African Institute of Chartered Accountants (SAICA) and the Johannesburg Stock Exchange (JSE). The terms of reference for the King Committee (named after its chair, Judge Mervyn King) included both the financial and ethical dimensions of corporate governance (Rossouw, van der Watt & Malan, 2002). South Africa's corporate governance reforms now centre around four reports, namely King I issued in November 1994, the King II issued in March 2002 (West, 2006), the King III issued in 2009 and lastly King IV issued in November 2016.

The notion of corporate governance and the development of corporate governance guidelines and codes has been a prominent feature in South Africa's business environment since the early 1990s (Marx, 2008). The reasons for its prominence are indicated by various researchers as:

- The need to restore confidence and trust in South African institutions following the apartheid era (Burke & Clark, 2016);
- The need for robust market discipline and corporate reform to attract and retain foreign investors (Marx, 2008; Maseko, 2015);
- The expectation for South African companies to play a role in addressing the socio-economic challenges facing the country (Croucher & Miles, 2010); and
- The call to respond to the first corporate governance code issued in the UK, namely, the Cadbury Report of 1992 (Marx, 2008; Miles & Jones, 2009).

A 'modified' Anglo-American model of corporate governance has been evolving in post-apartheid South Africa as a consequence of the King reports and social pressures (Andreasson, 2011). The King reports have the potential to act as a catalyst for a hybrid model of corporate governance in South Africa that is characterised by combining shareholder and stakeholder interests and anchoring these interests in 'African values'. Such a model would enhance the stability and legitimacy of South Africa's economic system in what remains a volatile socio-political climate. A successful hybrid model must be capable of addressing both shareholder and stakeholder concerns and to effectively anchor these concerns in a cultural framework that confers popular legitimacy on the system as a whole (Andreasson, 2011). This is supported by Rossouw (2005), who states that the dominant model of corporate governance that emerges in these national codes is an inclusive model of corporate governance in which boards of directors are not merely accountable to shareholders but also responsible to all other stakeholders of the company.

The hybridisation of South African governance is a result of tensions between a traditional liberal emphasis on individual property rights imbued in the Anglo-American model and the communitarianism inherent in the concept of 'African values' or *Ubuntu* (West, 2006). *Ubuntu* denotes an African humanism emphasising empathy, understanding, reciprocity, harmony and cooperation and it constitutes a potential guiding principle for organising African societies and measuring well-being (Prinsloo, 1998).

Below is a detailed discussion of the four King Reports.

King I

The first King Report on Corporate Governance (King I) was published in 1994. It was considered ahead of its time (Marx, 2008) as it set an international benchmark for standards and best practice (Jansen van Vuuren & Schulschenk, 2013). King I drew extensively on the Cadbury Report and similarly adopted a self-regulatory approach of 'comply or explain' (Mangena & Chamisa, 2008). This meant that companies that complied with the report needed to disclose their level of compliance and, in instances where they did not comply, explain their reasons for non-compliance.

The report was, however, different from its British counterpart insofar as it looked beyond financial and regulatory facets; it was the first to successfully conceptualise the need for companies to acknowledge the society and the environment in which they operate as inseparable components of value creation (IoDSA, 2002).

King I addressed the need for increased transparency and segmental disclosures required of local companies to counter declining ethics within the corporate environment. It also introduced measures to prevent non-executive directors, who represent the majority of shareholders, from overpowering the interests of the minority shareholders (Crous, 2017).

In 1995, the JSE adopted King I and effectively, all listed companies on the securities exchange were required to comply with the recommended principles (Crous, 2017). While the report drew unprecedented interest in South Africa's corporate governance landscape (Rossouw, van der Watt & Malan, 2002) and was hailed as a potential catalyst to enhance the stability and legitimacy of South Africa's economic systems (Andreasson, 2011), various researchers highlighted the shortcomings of King I (Kakabadse & Korac-Kakabadse, 2002; Marx, 2008; Maseko, 2015):

- It encouraged a 'tick-box' approach to compliance;
- It put too much emphasis on disclosure rather than encouraging best practice as its main incentive;
- It protected the vested interests of corporate groups in South Africa; and
- It lacked wider consultation, did not invite public discussion, did not draw on external expertise and thus did not directly address issues of corporate governance.

The report was criticised for two other shortcomings:

- Transparency and disclosure of certain issues appeared to be lacking in most South African companies, with only the top 30 or 40 JSE-listed companies introducing certain performance measures. By and large, investors were given little information to adequately assess the performance of the different units across the companies (Kakabadse & Korac-Kakabadse, 2002).
- The report did not address Information Technology (IT) issues. Maseko (2015) excuses the absence of IT governance in the report as at that time, IT was regarded as an enabling function rather than a strategic function, and hence it was not yet a critical issue worth addressing in any great detail.

In response to the above criticisms as well as the need to evolve with global trends, the IoDSA decided to review King I. This resulted in King II (Maseko, 2015; Crous, 2017).

King II

King II was drafted in 2001 and issued in 2002. Its effective date of implementation was 1 March 2002. Vaughn and Ryan (2006) and Marx (2008) described it as a more comprehensive report, building on the foundation laid by its predecessor. King II maintained its original stance and was not in favour of legislation which forced companies to comply with its recommendations but rather, it stayed true to the ethos of self-regulation (Miles & Jones, 2009). However, the report expanded on its 'inclusive approach' to corporate governance, recommending the introduction of 'triple bottom line' reporting to incorporate the economic, environmental and social aspects of a company activities (Miles & Jones, 2009; Hendricks & Wyngaard, 2010). It put a stamp on theme introduced in King I, stressing that companies ought to recognise that they do not exist independently of the society in which they operate and, although the primary duty of governing bodies is to protect the interests of the shareholders, the interests of other stakeholders such as the community, customers, employees and suppliers all need to be considered when developing company strategy. As a result, King II was hailed for its enhanced focus on transparency and disclosures of non-financial information through the adoption of integrated reporting which, according to Crous (2017), had not been included in any other corporate governance codes and documents around the world.

Furthermore, King II motivated its push for more inclusive corporate governance practices by reinforcing the idea that companies which embraced inclusivity and demonstrated concern for non-financial issues were more likely to build an atmosphere of trust and a better understanding of their corporate objectives amongst stakeholders. This meant that, when the next crisis comes (and these are inevitable for big companies) there will be a greater goodwill to help the company survive (IoDSA, 2002).

While the King Committee went to great lengths to overcome some of the criticism levelled against King I (Maseko, 2015), King II was nonetheless criticised for its self-regulatory nature as well as the lack of enforcement through statutory channels (Marx, 2008).

King II was reviewed in 2009 and subsequently, King III was introduced (IoDSA, 2009).

King III

King III came about as a result of the new Companies Act of 2008 and changes in international trends in governance (IoDSA, 2009). King III, which was initially issued in 2009, promoted an integrated approach to governance and reporting, providing extensive guidance on integrated reporting and disclosures of governance-related matters (PwC, 2009; Maseko, 2015).

Unlike its predecessor, King III was applicable to all entities irrespective of their size or whether they were listed or not. However, it placed no statutory obligation on companies to comply with its recommendations and principles, thus moving away from the traditional ‘comply or explain’ approach to an ‘apply or explain’ basis of reporting (PwC, 2009). This allowed governing bodies to apply the recommendations differently or to apply other practices, when they considered such practices to be in the best interests of the company while still abiding by the overarching principles of fairness, accountability, responsibility and transparency. However, according to Walker and Meiring (2010), proper compliance required adequate explanation of how the principles and recommendations were adopted and applied or, in cases where they were not applied, the reasons for deviating from best practice.

Among the emerging governance trends and issues incorporated into King III were alternative dispute resolution, risk-based internal audit, shareholders’ approval of company remuneration policy, board evaluations, business rescue and importantly, an expansion of IT-related matters, with a chapter on IT governance (IoDSA, 2009).

Turel and Bart (2014) state that as technology continues to increase in strategic importance and concomitant risk to companies, the rapid deployment of emerging technologies within companies can have a significant impact on sustainability. Thus, IT governance should be an integral part of corporate governance, which justifies its inclusion in the report.

One critical consideration is that although King III addressed IT governance extensively, it did not provide any guidance on simplifying IT governance disclosures. Instead companies were only required to disclose their application of the principles and recommendations (IoDSA, 2016).

As a result of the significant changes in both business and society and to address the shortcomings of King III, King IV was introduced in 2016.

King IV

King IV was published on 1 November 2016. The report replaced King III altogether and is applicable to companies with financial years commencing on or after 1 April 2017 (IoDSA, 2016). According to Deloitte (2016), King IV takes a bolder approach than King III insofar as:

- The report follows a principle-based and outcome-based approach as opposed to being rule-based. This is consistent with current global opinions which advocate heightened accountability and transparency. It also recommends that practices ought to contribute to the performance and sustainability of a company;
- The report is resolute in its unyielding effort to reinforce the idea that corporate governance should be seen as a holistic set of arrangements that embraces ethical leadership, attitude, mindset and behaviour; and
- The report continues to stress increased transparency and targeted disclosures in all areas.

From an application perspective, King IV is a framework which can be adopted across listed and unlisted companies, profit and non-profit as well as public and private entities (IoDSA, 2016).

King IV steps away from the 'apply *or* explain' approach and recommends an 'apply *and* explain' approach, relieving governing bodies of the burden of compliance by reducing the 75 recommended practices in King III to 16 basic principles. These 16 principles can be adopted by any company and are all necessary to substantiate the practice of corporate governance (IoDSA, 2016). The required explanation gives effect to each principle and enables stakeholders to make an informed decision as to whether a company is well governed or not. The explanation also helps in shifting the focus of companies from a compliance mindset to a qualitative mindset, which encourages the achievement of objectives through careful consideration of the entity's circumstances (IoDSA, 2016; Piek, 2016).

The principles addressed in King IV include the following:

i. The governing body should lead ethically and effectively.
ii. The governing body should govern the ethics of the organisation in a way that supports the establishment of an ethical culture.

iii. The governing body should ensure that the organisation is—and is seen to be—a responsible corporate citizen.

iv. The governing body should appreciate that the organisation's core purpose, its risks and opportunities, strategy, business model, performance and sustainable development are all inseparable elements of the value creation process.

v. The governing body should ensure that reports issued by the organisation enable stakeholders to make informed assessments of the organisation's performance and its short, medium and long-term prospects.

vi. The governing body should serve as the focal point and custodian of corporate governance in the organisation.

vii. The governing body should comprise the appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively.

viii. The governing body should ensure that delegation within its own structures promotes independent judgment and assists with balance of power and the effective discharge of its duties;

ix. The governing body should ensure that the evaluation of its own performance and that of its committees, its chair and its individual members, promotes continued improvement in its performance and effectiveness;

x. The governing body should ensure that the appointment of and delegation to, management contribute to role clarity and the effective exercise of authority and responsibilities;

xi. The governing body should govern risk in a way that supports the organisation in setting and achieving its strategic objectives;

xii. The governing body should govern technology and information in a way that supports the organisation setting and achieving its strategic objectives;

xiii. The governing body should govern compliance with applicable laws and adopted, non-binding rules, codes and standards in a way that supports the organisation being ethical and a good corporate citizen;

xiv. The governing body should ensure that the organisation remunerates fairly, responsibly and transparently so as to promote the achievement of strategic objectives and positive outcomes in the short, medium and long term;

xv. The governing body should ensure that assurance services and functions enable an effective control environment and that these support the integrity of information for internal decision-making and of the organisation's external reports;

xvi. In the execution of its governance role and responsibilities, the governing body should adopt a stakeholder-inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the organisation over time;

xvii. The governing body of an institutional investor organisation should ensure that responsible investment is practised by the organisation to promote the corporate governance and the creation of value by the companies in which it invests (IoDSA, 2016).

King IV also includes specific sector supplements for municipalities, non-profit organisations, retirement funds, small and medium enterprises and state-owned entities. These sector supplements are primarily aimed at the governing body of these entities, as it is the focal point of corporate governance within the organisations (IoDSA, 2016). Unfortunately, there is no sector supplement for auditing firms. More details about the 17 principles can be found in Annexure H.

The next section discusses any legislation, codes or guidelines available for auditing firms in South Africa, if any.

2.4.1.1 Legislation applicable to all auditing firms in South Africa

In South Africa there is no specific corporate governance code for auditing firms. As stated above, the King IV Code is applicable to all types of organisations. South Africa has the APA which provides guidance for auditing firms. To develop a corporate governance code for South African auditing firms, one would have to ensure that the code stays within the guidelines of the applicable Act, as the code cannot contradict the Act. Accordingly, the following section discusses the APA in South Africa and any regulations on the governance structure of auditing firms that would have to be considered when drafting guidelines on corporate governance practices and oversight structures for auditing firms.

2.4.1.1.1 The Audit Profession Act (APA) in South Africa

The APA of 2005 in South Africa provides information on the establishment of the IRBA, the education, training and professional development of registered auditors, the accreditation of professional bodies, the registration of auditors, the regulation of the conduct of the registered auditors, repealing an Act and providing for matters connected therewith (APA, 2005). This Act consists of seven chapters:

- Chapter 1: Interpretation and objects of Act
- Chapter 2: IRBA
- Chapter 3: Accreditation and registration
- Chapter 4: Conduct by and liability of registered auditors
- Chapter 5: Accountability of registered auditors
- Chapter 6: Offences
- Chapter 7: General matters.

From the above it can be seen that there is no specific chapter in the APA that provides information or guidance on the governance of auditing firms. Chapter 2, Part 4 provides details on the governance of the regulatory board, which in this case is the IRBA.

Chapter 3 section 38 of the APA, discusses the registration of firms as registered auditors. According to the APA 26 of 2005, the word ‘firm’ means a partnership, company or sole proprietor. King IV clarifies that it is intended to apply to all organisations, regardless of their form of incorporation. The main objective of King IV is to broaden acceptance of corporate governance by making it accessible and fit for application across a variety of sectors and organisation types (IoDSA, 2016). In pursuit of this goal, King IV contains supplements for specific sectors. There is, however, no sector supplement specifically for auditing firms.

Chapter 3 section 38 also states that the only firms that may become registered auditors are (1) partnerships of which all the partners are individuals and are themselves are registered auditors, (2) sole proprietors where the proprietor is a registered auditor, (3) companies which comply with sub-section 3. This sub-section states that a company may be registered as a registered auditor if it has share capital and its memorandum of incorporation provides for directors and past directors to be liable, jointly and severely, together with the company, for its debt and liabilities contracted during their period of office. Only individuals who are registered auditors are shareholders of the company; every shareholder of the company is its director (APA, 2005).

From the above it is clear why many auditing firms in South Africa struggle to find independence on their governance structures. As stated above, all directors must be registered auditors. This means that directors would be experienced auditors, who would most probably not be independent of the firm and its clients. This regulation will have to be taken into consideration when the corporate governance code for auditing firms in South Africa is developed.

Summative comment on corporate governance codes in South Africa

In 1994 the first corporate governance report, King I, was released. This report was named after Mervyn King, the chair of the IoDSA who commissioned the report. King I was reviewed in 2002 and King II was issued. In 2009, the Report was reviewed again and King III was issued. King IV was issued in November of 2016 and is applicable in South Africa. The King reports combine the shareholder and stakeholder theories. King IV consists of 17 principles and adopts an ‘apply and explain’ model. Its principles can be adopted by any company (including an audit firm), and are compulsory for listed companies. South Africa does not have a corporate governance code specifically for auditing firms and the APA does not provide any guidance on this topic. King IV also does not have a sector supplement which can be specifically applied to the auditing firms in South Africa.

Critical link to the objectives of the study

Corporate governance codes (such as those mentioned above) were developed due to corporate collapses, business failures and fraudulent financial reporting. Regardless of these codes, however, corporate failures still happen. This literature review was necessary to identify the corporate governance principles that are applied in each of the countries selected for the study. From the above it is clear that there is only one corporate governance code that is applicable to auditing firms, and this code can be found in the UK. The USA, Australia, the Netherlands and South Africa all have excellent corporate governance codes, but there is no specific code for auditing firms in these countries.

As stated above, the APA does not contain guidelines on the corporate governance of auditing firms. The Audit Firm Corporate Governance Code of the UK can mostly be applied to auditing firms and thus this code, together with King IV, will be used to develop a checklist and questionnaire for the empirical study. It will also provide guidelines on corporate governance practices and oversight structures for auditing firms in South Africa.

2.5 International audit standards providing guidance on audit firm governance

2.5.1 ISQC 1 and ISA 220

ISQC 1 addresses Quality Control for Firms that Perform Audits and Reviews of Financial Statements and Other Assurance and Related Services Engagements. It is applicable to all auditing firms in the world. The IAASB's ISQC 1 was issued in 2009. It recognises the role of external communication in a system of quality management and that a firm's external reporting obligations could be established in law, legislation or professional standards in different jurisdictions. It further anticipates that the firm will communicate relevant information about its system of quality management to relevant external parties (IRBA, 2018).

There are eight components that are relevant to an auditing firm's system of quality management and provide a necessary link to the management of quality at the engagement level:

i. Governance and leadership;
ii. The firm's risk assessment process;
iii. Relevant ethical requirements;
iv. Acceptance and continuance of client relationships and specific engagements;
v. Engagement performance;
vi. Resources;
vii. Information and communication; and
viii. Monitoring and remediation process.

From the above eight components, the governance and leadership requirement is discussed in detail below, as this has a direct link with the 'tone at the top' in auditing firms that the study addresses.

Governance and Leadership

The IAASB believes that governance and leadership of an organisation is of vital importance to quality of service, as it is the way the company envisions its culture and ethics. It is also the basis of how decisions in the business are made. Governance of a firm often influences the understanding of the firm by the public; and a firm without successful governance structure may be viewed as one that does not work in the public interest (IRBA, 2018).

ISQC 1 has been greatly improved to improve the robustness of the governance and leadership of companies. It discusses, in particular, the expected actions of firm leadership in setting the tone at the top, the required leadership skills and keeping leadership accountable through performance assessments. The norm also now discusses the impact of the company's strategic actions, including financial and operational decisions on quality of service and the role of the company in the public interest, as well as the capacity of firm leadership to influence decisions about the company's resources (IRBA, 2018).

The ISA 220 deals with the specific responsibilities of the auditor regarding quality control procedures for an audit of financial statements. It also addresses, where applicable, the responsibilities of the engagement quality control reviewer (IAASB, 2010).

ISQM 1 and ISQM 2 were released by the IAASB in 2019, but they have not been implemented as yet. The Exposure Draft of ISQM1 (ED-ISQM1) states that the extant ISQC 1 does not specifically address firm governance nor does it contain much detail as to what is expected from firm leadership in relation to firm governance. It therefore includes various suggestions to address firm governance and enhance the role of firm leadership in sustaining and continually improving audit quality (SAAPTI, 2020). Because the ISQM is still in draft format, it is excluded from this study.

The above discussion confirms the statement in section 2.1 that many codes, acts and legislation address the quality control of the audit firm, but very few specifically address the corporate governance of the auditing firm. This study aims to close this gap and to add to the literature on corporate governance of auditing firms.

2.6 Comparison of the UK audit firm governance code and King IV

As stated above, it is clear that there is only one corporate governance code that is applicable to auditing firms, and this code can be found in the UK. The USA, Australia, the Netherlands and South Africa all have sound corporate governance codes, but there is no specific code for auditing firms in these countries.

As indicated in Annexure D, in 2016 the FRC conducted a study to examine the UK Corporate Governance Code to determine how it could be applied to auditing firms (as well as how it was potentially already incorporated in the UK Audit Firm Governance Code). This analysis indicated that the Audit Firm Governance Code already included most of the principles contained in the Corporate Governance Code. Like King I, when it was initially developed, King I drew extensively on the Cadbury Report and similarly adopted a self-regulatory approach of ‘comply or explain’ (Mangena & Chamisa, 2008). It could be argued that the UK Audit Firm Governance Code could be used as the foundation and benchmark for developing corporate governance guidelines for South African auditing firms. For this reason, the present study compares the UK Audit Firm Governance Code to King IV. As there are significant similarities, it would be possible to use King IV to further develop a sector supplement for auditing firms in South Africa and include it in future King iterations. A summary of this comparison is shown below.

Table 2.2: Comparison between the UK Audit Firm Governance Code and King IV

UK Audit Firm Governance Code Principles	**KING IV principles that address the same principle as the UK Code**
Leadership	Principles 6, 7, 9 and 10
Values	Principles 1, 2, 16
Independent non-executives	Principle 7
Operations	Focuses on auditing firms, thus not applicable in King IV
Risk Management	Principle 11
Reporting	Principles 5, 11, 8
Dialogue	Principle 16

Own comparison

A more detailed comparison can be viewed in Annexure I of the study. This comparison contributed significantly to the development of the checklist and questionnaire to be used in the data collection of the empirical evidence.

2.7 Conclusion

In this chapter a detailed literature review was performed on corporate governance, corporate governance theories and the development of corporate governance in the UK, USA, Australia, the Netherlands and more specifically, South Africa. The chapter also examined literature on the governance of auditing firms.

Corporate governance consists of a set of principles, namely, legitimacy and voice, direction, performance, accountability and fairness. For the purposes of this study, corporate governance was defined as "a set of responsibilities and practices instituted by the governing body in order to direct a company to achieve its strategic objectives while remaining sustainable, accountable and transparent and acting in the best interest of all the stakeholders".

Corporate governance is often described in terms of two seemingly opposing models—the shareholder and the stakeholder models. The shareholder model deals with situations where one person, the principal, wishes to induce another, the agent, to perform some task that is in the interests of the principal but not necessarily of the agent. The stakeholder model is based on the corporate perspective of a private organisation that is accountable to a range of stakeholders, such as owners, vendors, consumers, staff, management, government and local communities. These two models are also known as one-tier and two-tier board structures.

Corporate governance codes arose out of deep-seated concerns stemming from well-publicised corporate failures. In the UK, the 2018 Combined Code is currently the effective corporate governance code. This Code consists of five principles, which are applied on a 'comply or explain' basis. In the USA the SOX is the corporate governance legislation. This is not a voluntary code, but rather legislation. The Act contains 11 titles that range from corporate board responsibilities to criminal penalties. The Corporate Governance Report applicable in Australia consists of eight principles and is applicable to all listed entities. In the Netherlands, the 2016 Dutch Corporate Governance Code consists of five chapters, which contain 24 principles. This code is based on the stakeholder approach. In South Africa, King IV is currently the effective corporate governance code. King IV consists of 17 principles and recommends an ‘apply and explain’ approach. The principles can be adopted by any company.

Auditing firms are the guard dogs of the financial sector, yet there is very little legislation, standards or codes that govern the corporate governance structures of auditing firms. The APA of 2005 provides information on the governance of the regulatory board, but not specifically the auditing firm. The Act states that an auditing firm can be either a partnership, a company or a sole proprietor, which means that King IV could be applied to an auditing firm as well. ISQC 1 and ISA 220 provide information on the governance and leadership and ethical requirements of an auditing firm. The information is, however, very limited, with no detailed guidelines on audit firm governance. The UK’s Brydon Report emphasises the principles of corporate auditing and the importance of acting in the public interest. This report, like most other acts, reports and codes, focuses more on the governance of the individual auditor rather than the auditing firm specifically. The UK Audit Firm Corporate Governance Code of 2010 is designed specifically for auditing firms. From 2014 to 2015, this Code was reviewed and several changes were made. The Code consists of six principles: (1) leadership, (2) values, (3) independent non-executives, (4) operations, (5) reporting, (6) dialogue. The FRC performed a study to determine which principles in the UK Corporate Governance Code could be applied to auditing firms and found that Chapters 1 to 3 were suitable for auditing firms.

Because South Africa has a strong colonial legacy and resultant ties with UK, its “corporate law and corporate practice have been adopted mainly from the UK” (West, 2006, p. 435). A similar analysis is thus performed in Chapter 6, to determine how King IV can be applied to South African auditing firms. As the UK already has a corporate governance code specifically for auditing firms, this code together with King IV, will also be used as a guideline to establish which principles could be applied to provide guidelines on corporate governance practices and oversight structures for auditing firms in South Africa.

The following chapter discusses well-known corporate failures and audit failures in the UK, USA, Australia, the Netherlands and South Africa.

Chapter 3: CORPORATE FAILURES AND AUDIT FAILURES

3.1 Introduction

The purpose of this chapter is to provide a literature review on how the lack of corporate governance has contributed to some of the worst financial corporate failures in the UK, USA, Australia, the Netherlands and South Africa, and in particular, to determine whether poor corporate governance practices at auditing firms contributed to these failures. This chapter also explores the impact of weak corporate governance at auditing firms on the reputation and sustainability of these firms, possibly resulting in their failure.

As stated in Chapter 1, a 'scandal' is defined as a circumstance or action that offends propriety or established moral conceptions or disgraces those affected with it (Abdoul Fatahi, 2017). Toms (2019) defines a 'financial scandal' as a situation or event that has occurred as a result of financial resources being used in a morally questionable manner where there are serious consequences for third parties, which are widely known. An 'audit failure' takes place when an auditor indicates to the public that a client's financial statements are fairly presented in accordance with GAAP, when in fact they are not (Pearson, 1987). Most corporate scandals are the result of fraud and often lead to audit failures as well (Muraina, Okpara & Ahunanya, 2010). For the purposes of this thesis, a 'corporate failure' is defined as an event or situation involving the use of financial resources through questionable ethical behaviour, where management misrepresents financial statements and auditors fail to discover or report this misrepresentation, which then becomes public knowledge.

According to Bauer, Gunster and Ottten (2003), corporate governance has received considerable attention after corporate scandals such as Enron and WorldCom in the USA, Royal Ahold in the Netherlands and Carillion in the UK. According to the McKinsey Global Investor Opinion Survey, corporate governance is more important than the firm's financial performance for at least 15% of European investors. For companies that are well governed, at least 22% of institutional investors are willing to pay a premium of 19% for their investments. Well-governed companies have higher equity returns, are valued more and their accounting statements show better operating performance (Bauer et al., 2003).

According to Zerban (2018), good corporate governance can prevent corporate scandals as well as increasing the trust between society and business corporations. It also makes an organisation attractive to investors by enhancing its reputation and image. Todorovic (2013) concurs, stating that investors would rather invest in an organisation that practices sound corporate governance principles as this is likely to provide them with a good return on their investment.

Firth, Fung and Rui (2007) observe that companies with a greater number of independent directors who separate the roles of chairman and executive director have higher earnings. The greater the independence of the board, the higher the quality of accounting information. Ho, Aripin and Greg (2012) agree, stating that the financial performance of a company is better when the board of directors is independent. Many of the corporate failures that are discussed in this chapter confirm this statement, as many failed due to a lack of independence on the board or weak auditor independence.

According to Shinde, Willems, Sallehu and Merkle (2015), in the past few decades the media has been flooded with news on accounting scandals. This has resulted in the public calling for action to protect their interests. Individuals who invest money want the comfort of knowing that they are protected from fraud. These scandals have resulted in the development of many corporate governance codes (as discussed in Chapter 2). It is widely believed that audit failures are the result of corporate transgressions—as in the case of Arthur Andersen's failure with Enron. According to Shinde et al. (2015), the Enron vs Arthur Andersen failures were not the first time a lapse in auditing standards and procedures allowed a major corporation to commit fraud. Many other countries have experienced the same phenomenon. More detailed examples of this are provided in this chapter.

Despite numerous efforts and regulations to improve corporate governance as well as calls from the public to improve corporate governance at auditing firms, corporate failures and audit failures continue to occur. In many of these scandals, greed was the reason for the corporate fraud, together with a lack of accountability, transparency and weak ethical behaviour. Corporate governance aims to increase accountability, transparency and ethical behaviour, to avoid or detect problems before they occur and to ensure that the business is a success. If there is no corporate governance in an organisation, it is unlikely that unethical behaviour will be detected in time. Unfortunately, after many corporate failures, the accounting and auditing professions have lost the trust and confidence of the public and many individuals question their credibility (Zerban, 2018).

A lack of proper regulation, combined with auditing practices that share in company benefits as well as greedy partners are usually at the core of corporate accounting and auditing scandals. It is often the case that the auditor 'watchdogs' do not bark when they are supposed to (Zerban, 2018). Zerban (2018) predicts that more Enron-type scandals will occur if there is no drastic overhaul of corporate governance in auditing firms.

Accounting scandals obscure the reliability, understandability and comparability of financial information contained in financial statements. In accounting scandals, therefore, fraud committed on financial statements plays a significant role. This is especially the case for corporate fraud, primarily due to inadequate corporate governance implementation and internal controls. Following the accounting scandals in recent years, a large majority of stakeholders has begun to believe that independent auditing firms do not fully discharge their duties (Kizil & Kasbasi, 2018). Below is a detailed explanation of the corporate scandals and failures which took place in the UK, USA, Australia, the Netherlands and South Africa.

3.2 Corporate scandals and failures

The world has seen more than two decades of corporate failures and scandals such as falling stock markets, dubious accounting practices, fraud and the abuse of corporate power associated with global companies such as WorldCom, Arthur Anderson, Enron, Murray & Roberts, and more recently, Steinhoff and KPMG (Arjoon, 2005; Lungisa, 2017; Monahan, 2012). These acts of self-interest have undermined the confidence of all stakeholders, resulting in a relationship of broken trust between stakeholders and governing bodies (Arjoon, 2005; Monahan, 2012). According to Zerban (2018), there is usually not just one contributor to a failure, but many. Banks, regulators, management, accountants and auditors have all contributed to the failure of many corporate entities (Zerban, 2018). According to Leung and Cooper, (2003) the lack of effective corporate governance is one of the biggest reasons for most corporate failures. Such failures may be accompanied by 'creative accounting', a lack of independence of the audit function, regulation inadequacies and large and inappropriate management compensation. Dube (2008) agrees, adding that corporate failures worldwide were caused *inter alia* by insider loans, compensation scandals, falsifying financial statements, inefficient and unethical conduct by external auditors and closed decision-making. All of these factors have led to waste and corruption.

The next section discusses the corporate failures in the UK, USA, Australia, the Netherlands and South Africa. Each section also examines the role of auditors in the corporate failure and whether they contributed in any way to the scandal or failure.

3.2.1 Corporate failures in the UK

In the UK, accounting scandals ranged from the corporate failures of Barings Bank in 1995, Tesco in 2013, to the failure of Carillion in 2018, which went into liquidation without any warning signs, damaging investments of nearly £2 billion. The activities of these companies raised serious corporate governance issues. The role of company auditors was also concerning, as they failed to highlight red flags which would have indicated that the going concern of these companies was under serious threat (Awolowo, Garrow, Clark & Chan, 2018). Below is a detailed discussion of some of the corporate failures that took place in the UK.

3.2.1.1 Robert Maxwell (1991)

In November 1991, a successful business leader, Robert Maxwell disappeared at sea from his yacht, *Lady Ghislaine*. In the weeks following his disappearance, it emerged that his business empire had been in serious financial trouble for some time (Wearing, 2005). On 5 November 1991, Robert Maxwell, a media business empire in the UK, closed its doors after almost 40 years of activity (Clarke, 1993).

According to Smith (1992), Maxwell used four techniques to misappropriate funds from the companies under his influence. First, he pledged assets for additional loans as insurance. Yet instead of providing the assets to the lender, Maxwell sold the assets for cash. Secondly, he redirected shares and cash from MGN to Maxwell-controlled Bishopsgate Investment Management. Maxwell then promised these shares to his private companies as protection for more loans. Thirdly, with the cash obtained from pledging shares, Maxwell funded the share price of MCC and MGN. These purchases should have been done under stock exchange regulations, but they were never disclosed. Due to the banks' lending Maxwell money, Maxwell had to ensure that the share price was high in order to maintain his financial creditability. He sold options to Goldman

Sachs with a share price higher than the market value when the contract was written to further boost MCC's share price. Because of this, Goldman Sachs purchased shares at a lower current market price and realised they would be able to make a profit when they sold the shares at a higher price stated in the option later. In the end, Maxwell stole MGN cash. Upon MGN's flotation, £43 million was passed on to private investors in Maxwell. The public wanted to know who would be held responsible for what happened at Maxwell (Smith, 1992).

The Maxwell trustees blamed the auditors, Coopers and Lybrand, for failing to report Maxwell's misuse of the fraud and pension funds. The Joint Disciplinary Scheme eventually disciplined Coopers and Lybrand and some of their audit partners. In 2001, PwC (Coopers and Lybrand's successor firm) announced that after the controversy, they had made operational changes and acknowledged the recommendations raised in the Department of Trade and Industry report. PwC was charged a £3.5 million Mutual Disciplinary Scheme fine, as well as £68 million in an out-of-court settlement that was used to settle the liquidators and donated an undisclosed sum to the defrauded pension funds. PwC's credibility was in shreds following the scandal. In 1992, the Cadbury Committee stated that due to several financial scandals, specifically mentioning Maxwell, they were asked to report on corporate governance matters (Wearing, 2005).

3.2.1.2 Barings Bank (1995)

The collapse of Barings Bank in February 1995 proved to be a turning point in public attitudes to financial risk in the UK. The bank had been in existence for more than 200 years and still maintained close ties with the founding family. Barings was founded by Francis Baring, the son of a German immigrant, in the 18th century.

Barings continuously expanded until the end of the 19th century and extended its operations to South America. Under Lord Revelstoke's chairmanship, due to the speculative projects made in Argentina, the bank went almost bankrupt in 1980. Rivals like the Rothschilds and the Bank of England were well aware that such a crash could have consequences for the entire banking system and Barings was not allowed to go under. Barings was refinanced and reorganised into a limited company, from a partnership. The events of 1980 were a salutary lesson for the bank, which subsequently worked hard to restore its reputation in the banking world (Wearing, 2005).

During the 1970s and 1980s, as the capital markets became bigger and more complex. Barings responded by setting up Baring Securities to take advantage of new and lucrative opportunities. The separation of traditional merchant banking from the modern, more glamorous, brokerage activities appears to have led to tensions and conflicts within the Barings community. It is very likely that the group's problems in the 1990s could have been partially due to this clash of cultures and the fact that many people at Barings simply did not realise the potentially enormous losses that could arise from the selling of derivatives that were poorly regulated. Unfortunately, Baring Securities was to be the downfall of the company. Despite the bank's collapse in 1995, the name Barings persists, following the International Nederlanden Group's (ING) acquisition of the bank. ING Barings survives but the Barings family connection has been largely lost (Wearing, 2005).

The books of the Barings Bank were audited in Singapore by the local audit firm, Deloitte. In London, the Barings Bank London's books were audited by Coopers and Lybrand. After the fall of Barings, KPMG, who were named as liquidators, began proceedings against Deloitte in Singapore. In 2003, the London High Court found that Barings Bank officers were responsible for the failure, and identified illegal trading by Nick Leeson (is a former derivatives trader who became notorious for bankrupting Barings Bank), rather than Deloitte in Singapore. In 2003, Deloitte was forced by a High Court decision to pay only £1.5 million in damages as a result of negligence on reasonably technical grounds. This was a tiny fraction of the £131 million in damages that Barings initially requested. The case was eventually settled at the Court of Appeal in London in April 2004, when a settlement was reached by KPMG and Deloitte (Wearing, 2005).

3.2.1.3 Tesco (2013)

Tesco is known as a multinational British grocery and general merchandise retailer with headquarters in Hertfordshire, England (Tesco, 2018). It is the world's third-largest retailer on a gross sales basis (Reuters, 2011). In addition to being a market leader for groceries in the UK, Tesco also has stores in seven countries across Asia and Europe. Tesco was founded in 1919 in the form of market stalls by Jack Cohen (BBC, 2013). Tesco's stocks are traded on the London Stock Exchange and as of 22 April 2015, it had a market capitalisation of around £18.1 billion (*The Telegraph*, 2015). The business was subjected to fraudulent accounting practices which led to resignations. In 2014, the Tesco debacle and fraud were estimated at £250 million. Accounting pull-forward methods were used, indicating early registration and revenue reporting. It was also an illegal accounting procedure interpretation (Business Insider UK, 2017).

On 19 September 2014, a whistle-blower informed the new chief executive, Dave Lewis, that the company's first-half profit estimate, announced on 29 August, may have been overstated by £246 million. The whistle-blower, who was a member of the finance department, was concerned that his department was not receiving the full documentation related to commercial income (Kukreja & Gupta, 2016).

The CEO and Chairman were briefed by Tesco's General Counsel on the situation. On 22 September 2014, Tesco announced the overstatement of profits. As per the audited financial statements of Tesco for the year 2014–2015, the total overstatement of profit before tax for the year ended 22 February 2015 was £53 million and a total overstatement for the years prior to that was £155 million (Kukreja & Gupta, 2016).

PwC had audited Tesco since 1983. The threat of familiarity was remarkably high after a relationship of 30-plus years. Arguably, this may have compromised the auditors' independence in dealing with Tesco. Some reports also criticised the Tesco board for failing to have non-executives with relevant experience in the supermarket sector. Furthermore, there was a severe failure in corporate governance by not having a CFO for five months. Many believed that the audit committee should have reacted promptly and decisively to the issues related to commercial income that PwC had raised. PwC, for its part, could have been more robust in dealing with the audit committee regarding this issue. After 32 years, Tesco's external audit was put to tender and PwC mutually agreed that they would not take part in the tender. Tesco named Deloitte as its new auditors (Kukreja & Gupta, 2016).

3.2.1.4 BP (2010)

The 2010 BP Deepwater Horizon oil spill in the Gulf of Mexico highlighted concerns related to CSR and ethics in companies in general, and in large corporations in particular (Balmer, 2010). The BP oil spill was a failure of more than just environmental law and the functioning of government agencies tasked with regulating deepwater drilling; the philosophy of corporate law, corporate governance and CSR was likewise to blame for the disaster (Cherry & Sneirson, 2011).

BP moved from a prosperous, middle-of-the-pack oil company to one which was regularly ranked in the world's top ten most profitable multinational firms. The company was rated highly in terms of employee care and became a favourite of advocates of CSR (Cherry & Sneirson, 2011). Deepwater Horizon, a drilling rig owned by Transocean and leased by BP to explore the oil field of Macondo, exploded, caught fire and sank on 20 April 2010. The accident killed 11 employees although one supply ship rescued others from the rig. The well attached to the rig started spewing oil at an alarming pace into the Gulf of Mexico. After the event, BP was found to have sacrificed protection to reduce the amount of time and money spent excavating the well (Cherry & Sneirson, 2011). The spill included basic concerns about how businesses were run, how they portrayed themselves to the public and the objectives they intended to accomplish. The catastrophic explosion and oil spill at BP exposed a corporate culture that had routinely ignored safety and environmental standards for employees. BP had a weak safety record, with many injuries that could have been avoided through improved maintenance of their facilities and increased precautions (Cherry & Sneirson, 2011).

3.2.1.5 British Home Stores (BHS) (2016)

The collapse of BHS is considered one of the most controversial and noticeable retail failures (Meek, 2016). The department store chain, which was 88 years old, failed due to poor management, an inability to drive more sales and compete with other firms. BHS was founded in 1928, initially selling clothing and household products, but later extending to furniture, electronics, food and beauty products (Rankin & Fletcher, 2016). Sir Philip Green, a British businessman and the chairman of the Arcadia Group, a company which coordinates multiple clothing brands, bought the company in 2000. The company faced difficulties after 14 years of BHS being run by Green with just a short-term increase in earnings. Eventually, Green sold BHS for £1 to Dominic Chappell in March 2015. It was reported that Sir Philip Green extracted significant amounts of money during the ownership and left the company on life support. There were also those who criticised the new owner, Dominic Chappell, for his lack of retail experience and for having been declared bankrupt three times (Laurent, 2016).

Apart from questionable behaviour in the sale, there were numerous strategic errors which kept the company back. Having nearly half of its assets invested in the stock market, the company was affected by the financial crisis at that time. Unsurprisingly, shares fell dramatically and the company lost large sums of capital. Weak returns on investment had resulted in inadequate funds to finance already low-wage workers' pension plans. The company experienced a small boost in revenue until BHS was sold to Chappell, receiving a 3.6% increase in 2014. The chain store did not compete with other companies, but the declining interest of people shopping in High Street stores was significantly influenced by the increase in internet shopping. There was a long drought of investment years before the agreement with Chappell happened in 2015, which led to revenues dropping every quarter and resulting in continuous losses (Laurent, 2016).

The chain closed all of its department stores across the country, with the branches overseas being sold to the Al Mana Group of Qatar. Despite the fact that the UK lost one of its oldest businesses due to a lack of corporate governance, there was also a loss of 11,000 jobs (Laurent, 2016). Thousands of employees were still at risk of not being covered by the pension scheme, despite contributing annually. BHS itself had no money to tackle the problem of debt, struggling at £1.3 billion. It was possible that the funds would be sought from the Pension Security Fund, to which thousands of other pension schemes contribute, many of which were much smaller than BHS. The Work and Pensions and Industry and Innovation and Skills Committees concluded in their joint report that Sir Philip Green was aware of the repercussions and hurried to sell the company to Dominic Chappell, a buyer he knew was manifestly unacceptable (Curwen, 2016; Laurent, 2016).

The BHS controversy raised further questions about the state of corporate governance in the UK. The UK Prime Minister, Theresa May, concluded after a joint inquiry by numerous committees, that the nation needed to address corporate irresponsibility and reform capitalism to ensure that it worked for everybody, and not just the fortunate few. The powerful Institute of Directors (IoD) proposed that Theresa May should initiate a study of UK corporate governance in order to avoid similar cases in the future (Laurent, 2016).

Key contributing factors to the demise of BHS were weak leadership and personal greed (Parliament UK, 2016). BHS was guilty of reckless mismanagement, led by Sir Phillip Green, its selfish and irresponsible creator. Continuously poor financial performance and high-cost systems contributed to massive corporate debts and a £571 million pension shortfall (Fuller, 2016). Bad high-cost structure management can lead to a competitive disadvantage, which largely led to the failure (Slatter & Lovett, 1999).

Many asked why the auditors had not raised any concerns. PwC faced a 15-year ban and a six-figure fine from the FRC. PwC audited BHS's finances before its sale for £1 just a year before the department store chain collapsed. Steve Denison, who spent more than 30 years at PwC as a partner, faced a £500,000 fine from the FRC, which was subsequently reduced to £325,000. PwC faced a record £6.5 million fine alone, which was lowered from the initial sum of £10 million after PwC decided to settle. The audit firm was also heavily reprimanded and ordered to track and help its audit practice and to provide the FRC with detailed annual reports on the practice for the next three years. PwC stated that their audit work raised significant shortcomings and that it is important to learn the required lessons. The apologised that their work dropped well below their planned professional expectations. The heavy penalties against PwC came after the FRC stated that it would double fines for bad audit work by the major accounting firms to £10 million. Until then, the largest fine issued by the FRC had been £5.1milion, also to PwC, for its audit of RSM Tenon in 2011 (Butler, 2018).

3.2.1.6 Patisserie Valerie (2018)

Referring to Patisserie Valerie's failure, SAAPTI (2020) reported that the failure of the auditor to identify the company's fragility resulted in the loss of jobs, investments, pensions and tax revenues. The fall of the Patisserie Valerie was considered rapid and unforeseen by its Chairman, Luke Johnson. Johnson has attributed some of the responsibility for the debacle to his auditors, Grant Thornton, for failing to identify what was happening. It would appear that Johnson did not take any responsibility for the Patisserie's loss. The food industry had seen its share of poor results that could be related to poor leadership practices, such as in the case of Patisserie Valerie (Garrow, Somerset, Awolowo & Clark, 2019). Over recent decades, deceptive audits have been at the core of organisational failures. The scandal at Patisserie Valerie showed that company's accounting was not an accurate representation of its true financial position (Mujih, 2018).

3.2.1.7 Ted Baker (2018)

Ted Baker is a luxury, multinational clothing retailer with 3,600 employees, listed on the London Stock Exchange. Recently in 2018, the luxury retailer revealed that an accounting mistake was twice as high as previously believed, leaving it with a £58 million void in its balance sheet (Jolly, 2020; Sikka 2020). The overvaluation of £58 million suggested that 35% of the value of clothing, shoes and other products was overvalued (Jolly, 2020). On 2 December 2019, the company disclosed that inventories had been overstated by £20 to £25 million. These problems appear to have gone back many years. The profit for the company after tax for 2019 was £41 million. More than a year's gains were wiped with the write-off of the overstated inventory value. The overstated inventory allowed the firm to report higher profits and paint a rosy picture of its affairs (Jolly 2020; Sikka, 2020).

Ted Baker was audited by KPMG since 2001 and the auditors had always issued the accounts a clean health bill. The audit report dated 31 March 2019 suggested inventory valuation as an essential object, but indicated that nothing was wrong. The directors reported that on the basis of their audit work, the external auditors had not reported any discrepancies or misrepresentations in the financial statements. The accounts revealed that in 2019 KPMG had received fees amounting to £445,000 and £397,000 in 2018. Nothing was publicly documented about the time KPMG workers spent on audits, the size of its audit teams, substantial questions raised, answers from directors or audit work conducted to corroborate the assessment of the company's inventory (Sikka, 2020).

To investigate the overstatement of the inventory, Ted Baker hired Deloitte. Preliminary inquiries by the retailer indicated that the value of the stock it retained on 26 January 2019 had been overestimated. Ted Baker shares fell by nearly 10%. The findings of the accounting audit came after the banks had appointed Ted Baker advisors to conduct a business review in the face of concerns that its poor financial position could force it to seek capital support (Jolly, 2020).

During the time at issue, Ted Baker was audited by KPMG. Due to a conflict of interest over its work with the retailer, KPMG was previously issued with a reprimand and a £3 million fine. After reports of 'forced hugs' at the Ted Baker, its founder and former CEO, Ray Kelvin, resigned in March 2019. Kelvin refuted any claims of corruption. Since the beginning of 2019, the company's shares had already lost more than three-quarters of their value and around 90% of their value since reaching a peak in November 2015. The fall in share price also wiped millions of pounds off Kelvin's personal capital, who still owns 35% of the firm. Sales and profitability were also struggling for the retailer. In 2019, Ted Baker released four profit warnings and slumped in October to a first-half loss of £23 million, the first in more than two decades. Ted Baker stated at the end of 2019 that it had cut its pre-tax profit forecasts to just £5 million for the year ending 25 January 2020. Since then, Ted Baker has said that trading was below expectations over November and the Black Friday period and that they expected difficult trading conditions would continue (Jolly, 2020).

The Ted Baker episode forms part of a steady stream of failures in corporate governance, accounting and auditing. Executive directors continue to nominate their associates in the corporate world as non-executive directors, who almost always fail to supervise businesses. Auditors are also delivering bad audits but facing trivial penalties. Auditors are (re)appointed at company AGMs, but the resolutions are not followed by any audit process detail. Reports by the Competition and Markets Authority and Sir Donald Brydon have been published but even those guidelines have not been adopted.

3.2.1.8 Carillion (2018)

Carillion was the second biggest construction group in the UK, moving from a going concern to compulsory liquidation over the course of a weekend. Carillion employed approximately 71,600 individuals and had annual sales of £5.2 billion. The corporate failure occurred due to Carillion failing to meet huge debt commitments in 2017 (Loxley, 2018). Over-expansion resulted in debt, which led to cash flow problems and reduced profits. In 2017, the share price dropped dramatically, however, the government continued to support private businesses and awarded Carillion contracts amounting to £1.3 billion towards the end of 2017 (Loxley, 2018). Unfortunately, the profit and cash flow problems continued and in January 2018 the share price was only 7% of its May 2017 level and the company was liquidated. This meant that the government had to step in and look after the needs of the public that Carillion usually addressed (Loxley, 2018).

The collapse of Carillion brought the usual suspects into the spotlight. Senior executives prospered on over-generous pay packets; one was paid handsomely months after departing. Shareholders did not ask awkward questions as long as dividends were buoyant. Auditors did not raise issues about accounting methods that, in hindsight, inflated reported profits (Mabbet, 2018). Sweet (2018) concurs, stating that Carillion did not act alone in deceiving lenders and investors. Loxley (2018) maintains that issues regarding oversight by the auditors were also raised in the collapse of Carillion, again proving that Carillion did not act alone. The Big Four accounting firms (Deloitte, KPMG, EY and PwC), who all provided auditing and advisory services to Carillion and received £72 million in fees from the company the decade before its collapse, were accused of being involved in the scandal. Carillion's auditors of 19 years, KPMG, had approved the financial statements only 10 months before the liquidation. The question was raised, "How could KPMG not have realised this?" (Silver, 2017). According to Sweet (2018), KPMG had failed to identify Carillion's growing debts and their efforts to disguise their true financial position. KPMG countered that their 19-year relationship with Carillion had not affected their independence.

According to Loxley (2018), large auditing and consulting companies struggle to be objective and they are hardly ever held accountable for their failings. Sweet (2018) concurs, stating that the economy needs a competitive market for audit and professional services which engenders trust. He urged the government to consider breaking up the Big Four into more auditing firms and detaching auditing firms from those providing other professional services (Sweet, 2018).

In the Carillion failure, it is evident that the independence of the auditors contributed to the corporate failures.

Summative comment on UK corporate failures

In 1991 Robert Maxwell, the UK media empire closed its doors. Funds were misappropriated and the auditors (PwC) had failed to report the fraud and misuse of pension funds. In 1995, Barings Bank which had been in existence for more than 200 years, failed. Their auditors were Deloitte and Coopers and Lybrand. The bank failed mostly due to illegal trading. Deloitte was fined £1.5 million in damages as a result of negligence on reasonably technical counts. Much later, in 2010, the BP Deepwater Horizon oil spill took place in the Gulf of Mexico. This scandal emphasised the importance of ethical leadership. Tesco, a multinational grocery and merchandise retailer, announced in 2014 that profits had been overstated by £155 million. PwC had been Tesco's auditors since 1983 and it seemed that the 30-plus year relationship had affected their independence. In 2016, BHS failed due to poor management, raising questions about the state of corporate governance in the UK. The auditors of BHS, PwC, faced heavy penalties for their poor audit work. In 2018, Carillion, the second biggest construction group in the UK, collapsed. Their over-expansion resulted in debt and this led to cash flow problems and reduced profits for Carillion. KPMG were the auditors for 19 years and once again it was argued that the auditors' independence had been affected. The collapses of Patisserie Valerie and Ted Baker also took place in 2018. Sweet (2018) argues that the collapses did not happen due to the actions of the corporate companies alone, as the auditors had failed to raise issues about the accounting methods, speaking right to the core of corporate governance. As can be seen above, the auditor practiced poor corporate governance, which then contributed to the corporate failures.

3.2.2 Corporate failures in the USA

The revelations of serious accounting problems at several prominent companies such as Enron, WorldCom and Tyco at the start of the new millennium were watershed events. Following these scandals, a number of other companies admitted to having accounting problems of their own. The 2007–2008 global financial crisis culminated, among others, in the collapse of Lehman Brothers (Harber, 2018). Most of these companies experienced large stock price declines upon the announcement of their accounting problems. Several of the companies involved in these scandals (e.g. Enron and WorldCom) were forced into bankruptcy (Agrawal & Cooper, 2017). Investors, customers, suppliers and employees filed numerous lawsuits against many of these firms.

Below is a detailed discussion of some of the corporate failures in the USA that received the most media attention.

3.2.2.1 Mckesson & Robbins (1937)

The fraud at McKesson & Robbins that occurred in 1937 preceded the scandals of Enron and WorldCom by many years. According to Barr and Galpeer (1987), this corporate failure had a profound effect on auditing standards. The McKesson & Robbins scandal was also the first time that the public and government scrutinised and criticised the accounting profession (Barr & Galpeer, 1987).

In 1937, McKesson & Robbins faced a slump in their pharmaceutical industry. The board decided to turn the stockpile of synthetic drugs (valued at $4 million), which actually only existed on paper, into cash (Baxter, 1999). Since the inventory did not exist, Coster's (the head of McKesson & Robbins) only choice was to pay the cash himself and reduce the inventory, but this was the last resort for Coster. He attempted to persuade the company's director, Julian Thompson, to take out a loan but Thompson had to testify to McKesson & Robbins' financial statements before he could do so (Thompson, 1953). Thompson found that there was unpaid inventory worth $21 million in Canada (Thompson, 1953). This discovery led Thompson to uncover the McKesson & Robbins was a scam. In 1938 the fraud was reported to the NYSE and all trading in McKesson & Robbins shares was suspended. It was found that the illicit drug division had totalled $19 million in false assets (Lodge, 1987). There was also $9 million in receivables from false accounts and $10 million in non-existent inventories (Baker & Bealing, 2006). According to Business: New Accounting (1939), 20% of McKesson & Robbins' $86,556,270 total assets was a lie.

For more than a decade, Coster had been able to keep his true motives secret from all, resulting in McKesson & Robbins thriving while several other businesses struggled (Baxter, 1999). He committed suicide in 1938 and because he had lived this lie for so long, the names F. Donald Coster was graved on his headstone instead of his real name, Philip Musica. Very little of Coster's

$2.9 million was recovered, as much of the money was used to pay off former creditors (Thompson, 1953).

For fraud of this magnitude to take place, many individuals would have had to have been implicated. McKesson & Robbins' auditors, PriceWaterhouse, conveyed to the public that McKesson & Robbins was an organisation of good financial standing. Unfortunately, it was later found that the audits had not been performed with as much diligence as expected (Baxter, 1999). PriceWaterhouse had spent a great deal of time analysing the balance sheet but did not personally audit the quantities of inventory reported by management nor did they question management about other documents. Interestingly, they did not challenge any cut-off problems and the large inventory purchases made near year-end. The management of McKesson & Robbins also limited the amount of audit work that PriceWaterhouse should have performed while PriceWaterhouse failed to challenge this decision taken by McKesson & Robbins (Baxter, 1999).

It was found that although PriceWaterhouse had followed the widely agreed audit procedures (Baker & Bealing, 2006), very little attempt had been made to understand the business of crude drugs (Baxter, 1999). The fraud should have been identified by applying the appropriate audit procedures, but the auditing profession was still evolving at that time and therefore the fraud passed undetected (Doron, 2009). PriceWaterhouse could have done much more, according to the SEC, as they failed to make proper use of the evidence available to them (Baxter, 1999). PriceWaterhouse was cleared of any wrongdoing and they accepted no responsibility for the fraud that had gone on undiscovered at McKesson & Robbins (Edwards, 1956). Many commentators claimed the acts of PriceWaterhouse indicated the opposite, because they repaid McKesson & Robbins the audit fees to the amount of $522,402.29 (Baxter, 1999; Edwards, 1956).

The McKesson & Robbins scandal shone the spotlight on the auditing and accounting profession (Neuner, 1956). As with Enron, both auditors and accountants were labelled by the public as incompetent and immoral (Baxter 1999).

3.2.2.2 Enron (2001)

The Enron financial corporate failure highlighted the value of sound corporate governance in the USA. In the latter half of 2001, a Texas based company listed on the NYSE, namely, Enron

Corporation, filed for bankruptcy (Bottiglieri, Reville & Grunewald, 2009). With revenues of over $100 billion in 2000, Enron was a world leading paper, utility and communication company. In October 2001, Enron announced it had a $618 million net loss for the third quarter and it would reduce shareholder equity by $1.2 billion (Brickey, 2003). The following day, after this announcement, the SEC requested information from the Enron officials. Two days later, Enron notified their auditors, Arthur Andersen that the SEC had initiated an investigation into Enron's financial accounting practices. A few days later, the Arthur Andersen engagement team started destroying Enron-related documents (Brickey, 2003; Markoff, 2013). This corporate failure had spanned 10 years and resulted in the convictions of corporate officers and the auditing firm, Arthur Andersen. In 2002, the SOX (which was discussed in Chapter 2) was introduced after this corporate failure (Primbs & Wang, 2016).

During the investigation into the accounting practices at Enron, it was found that in order to maintain the company's good credit rating, the accountants had kept assets and liabilities off the balance sheet, with Arthur Andersen's acquiescence. They did this by taking advantage of a specific accounting structure, namely, special purpose entities (SPEs). According to accounting rules, if a company is a majority shareholder in another company, it must consolidate its financials with that company. However, when a company and an SPE transact, the financials of the SPE can be treated as independent if at least 3% of the SPE's total capital comes from outside equity investors and that 3% remains at risk throughout the transaction. Moreover, the independent owner of the SPE must controls the SPE (Primbs & Wang, 2016). If all these conditions are met, the gains and profits from the transactions with the SPE may be recorded and the assets and liabilities may be excluded from the balance sheet. It became clear that the Enron managers took advantage of this accounting structure and eventually set Enron up for its downfall (Primbs & Wang, 2016). Arthur Andersen approved Enron's bookkeeping practices (Markoff, 2013) and failed to detect these 'creative accounting' practices. According to Primbs and Wang (2016) the lack of governance at Arthur Andersen was striking.

It was later proven that the allegations of irregular accounting procedures and fraud between Enron and Arthur Andersen were true and that corporate failure resulted in Enron's share prices dropping from over $90 per share to just cents. This was also followed by the dissolution of Arthur Andersen, one of the largest accounting firms in the world at the time (Bottiglieri et al., 2009). Ben

Glisan, former Treasurer at Enron, was the first executive to be sentenced to prison since pleading guilty to criminal fraud and admitting to manipulating Enron's financial statements. He was sentenced to five years in prison and also faced a fine of $900,000. Before joining Enron, Glisan had worked at Arthur Andersen, as had several other Enron employees. He partnered with Andrew Fastow and Michael Kopper at Enron to formulate collaborative arrangements that would strip Enron's balance sheet of billions of dollars of debt. Kopper had pleaded guilty in August 2002 to multiple Enron-related criminal charges. In January 2004, Fastow pleaded guilty to two counts of theft (Wearing, 2005).

The SEC eventually subpoenaed Arthur Andersen and the shredding of the documents stopped in November 2001. Unfortunately, by then literally tons of documents had already been destroyed that could have provided evidence of what exactly had occurred at Enron. The auditor was eventually convicted of obstruction of justice for destroying the documentation (Markoff, 2013).

As it turns out, the shareholders of the Enron era did not have the power to ensure that their interests would be completely taken into account by the senior management. While there was no specific explanation of what had gone wrong, the root of the scandal can be traced to a deterioration of the governance relationship between shareholders, the board and senior management. The failure provided valuable lessons for those with a vested interest in the shareholder-focused capitalist system, namely, shareholders, brokerage, auditors, financial regulators and policymakers, whose reaction has been swift. Officials immediately sought to locate the defects in the governance relationship which had enabled the most egregious malfeasance, however, they simply introduced 'patches', mostly in the form of updated rules or voluntary codes, to deter or avoid similar future scandals. Nearly all of the post-Enron efforts had the primary purpose of increasing the accountability of corporate executives to their boards and shareholders (Heath & Norman, 2004).

SOX created the PCAOB to try and prevent such behaviour by accountants and auditors. SOX focused largely on auditor independence and accountability. According to SOX, auditors may not provide non-audit services to their audit clients simultaneously. In the case where both auditing and consulting work is required by one client, the company's audit committee must pre-approve this and such approval of non-audit consulting services must be disclosed to all stakeholders of the company (Primbs & Wang, 2016).

The collapse of Enron and Arthur Andersen in 2001 is considered one of the greatest financial scandals in American history, undermining public trust in the work of independent auditors (Hopkins, 2016; Thomas, 2002). The public felt that these corporate failures were the result of audit failures and that the independence of auditors was an ongoing threat (Baker & Bealing, 2006). The Big Five accounting firms at the time promised to improve their disclosure to the public, but this was seen as too little, too late (Thomas, 2002).

The Enron failure displayed a stark lack of corporate governance within the auditing firm, Arthur Andersen, where once again independence played the biggest role. As stated above, there was a lack of independence and this resulted in the two entities colluding, ultimately leading to the failure of both Enron and Arthur Andersen.

3.2.2.3 WorldCom (2002)

Enron, the biggest financial failure in the history of the USA was soon overshadowed by the corporate failure of WorldCom (Brickey, 2003), the fourth-ranked telecommunications company (Pandey & Verma, 2005). WorldCom's far less state-of-the-art accounting fraud resulted in increased investment returns, massive financial disasters and similarly far-reaching civil and criminal investigations (Brickey, 2003). WorldCom's organisational collapse had arisen in 2002. WorldCom raised its assets by $11 billion, through capitalising carrier line costs, rather than expensing them. Arthur Andersen was also the external auditor of WorldCom (Hopkins, 2016).

The WorldCom corporate failure raised several questions regarding corporate governance, ethical leadership and unethical practices. Following this collapse, creditors, pension funds, banks and the economy were in turmoil. The company subsequently appealed to the USA court for reorganisation under Chapter 11 of the USA Insolvency Code and under the leadership of the new CEO, Michael Capellas, the new company (MCI WorldCom) not only reconsolidated its financial status, but also overhauled all its internal processes and turned it into an ethical company (Pandey & Verma, 2005).

An investigation into the WorldCom corporate failure found that it had overstated profits by more than $3.8 billion in 2001 and the first quarter of 2002. When this was announced, financial analysts were stunned. It also had a noticeable impact on financial markets. The press described this unethical WorldCom accounting practice as scandalous and it was immediately questioned why Arthur Andersen had not identified it. On 21 July 2002 WorldCom filed for bankruptcy protection. On 8 August, the company announced that it had also manipulated its capital assets in recent years, costing another $3.8 billion. The SEC charged the company with major accounting fraud on 26 June 2002 and immediately issued a court order prohibiting the company from destroying financial documents, restricting its compensation to current and former executives and ordering an independent company to monitor WorldCom. The House Committee on Financial Services held hearings on 8 July and the Senate Committee on Trade, Technology and Transportation held hearings on 30 July and many business officers were charged (Lyke & Jickling, 2002).

The circumstances under which the fraud at WorldCom had occurred were brought to light were similar to the account of Sherron Watkins, the Enron whistle-blower. Like Sherron Watkins, Cynthia Cooper, the Vice President of Internal Auditing at WorldCom, also exposed and corrected a massive accounting fraud (Brickey, 2003). According to initial accounts, in May 2002, the internal auditor of WorldCom, Cynthia Cooper, discovered the treatment of line costs as capital expenditures. The auditor discussed the misclassification with then CFO, Scott D. Sullivan and then-company Controller David F. Myers. Ms. Cooper referred the matter to WorldCom's board of directors' head of audit committee, Max Bobbitt, who in turn asked the company's current external auditor, KPMG, to investigate. The CFO was asked to explain the treatment and was fired after further discussions on the same day. WorldCom issued its public announcement on 25 June and on the very same day, David Myers resigned too. The chairman of the House Energy and Commerce Committee, Representative Tauzin, said on 15 July that the executives at WorldCom had realised as early as 2000 that the accounting treatment was unacceptable.

Arthur Andersen claimed in its 2001 audit opinion that the balance sheets and income statements fairly represented the financial position of WorldCom and were consistent with the GAAP in the USA (Zekany, Braun & Warder, 2004). According to Zekany et al. (2004), WorldCom's board of directors had been much too passive and management and had independent auditors failed to come forward. Arthur Andersen acknowledged that WorldCom's management did not completely comply with them, but still did not communicate their concerns to the Audit Committee. The internal audit team was also found distracted and understaffed.

One concern about WorldCom was why finding the misclassification took the company's internal auditors more than a year; this should have been found sooner, given the amount of expenses being capitalised (around $750 million per quarter) and the effect it had on net income and assets. To certain analysts, the fact that Arthur Andersen had not been told that line expenses were being capitalised was meaningless, as they claimed that Arthur Andersen must have formulated their audit to identify misclassifications of this extent. Some observers also note that Arthur Andersen should have taken into account WorldCom's increasingly precarious financial condition and heeded the possibility of aggressive accounting practices (Brickey, 2003; Lyke & Jickling, 2002).

The WorldCom scandal has come to be seen not only as a classic case of accounting fraud and organisational failure but also as a reference case for ethical leadership failure (Pandey & Verma, 2005). The WorldCom case highlights topics such as ethical leadership, ethical work culture and corporate governance (Pandey & Verma, 2005).

3.2.2.4 Tyco (2002)

The Tyco scandal occurred in 2002. Tyco management stole $150 million from illegal stock sales. Tyco's external auditor was PwC (Hopkins, 2016). Of all the businesses that came under post-Enron scrutiny, none felt the glare more than Tyco (Greenburg, 2002).

Tyco International was a major multinational company manufacturing a wide range of products, from computer devices to healthcare products and fire and safety systems. Tyco posted net sales of $14.50 billion for the 2004 fiscal year. In January 2002, concerns regarding the legitimacy and legality of Tyco's bookkeeping started to emerge when investors began asking difficult questions about their accounting (Greenburg, 2002). This led to a criminal investigation of Tyco's CEO, L. Dennis Kozlowski (Kay, 2002). Kozlowski, Mark Swartz, the CFO, and Mark Belnick, the Chief Legal Officer, were accused of behaving with self-serving and covert misconduct, systematically manipulating the corporation by raising over $170 million in loans without formal approval or consent from shareholders for themselves. Furthermore, Kozlowski and Swartz participated in lucrative party-related activities and were given luxurious rewards (SEC, 2005). Tyco's stock plunged by 61%, from nearly $60 a share to $23, erasing $70 billion in market value in less than nine weeks (Greenburg, 2002).

However, even before the Enron corporate failure, some questioned whether the vaunted growth of Tyco was genuine or whether, in some of its acquisition accounting, the firm had been manipulating its figures by being too aggressive. In 2000, Prudent Bear fund short-seller, David Tice, blasted Tyco for unfairly taking huge turnaround funds for its acquisitions (Greenburg, 2002). Tyco repeatedly and strongly denied doing anything that would raise profits in an artificial way. But it was not long before evidence surfaced that Tyco took measures to do just that in at least one case. The case involved a manufacturer of electronics called Raychem, which was acquired for $2.9 billion by Tyco in August 1999. While Raychem remained a single, small component in Tyco's corporate structure, it was a structure that included 2,000 offshore subsidiaries. These facts raised some suspicion (Greenburg, 2002). Regardless, the executive president of Tyco strongly defended the accounting of the company and stated that Tyco did not manipulate earnings and cash flow (Greenburg 2002).

This case unquestionably made headlines to the detriment of the company for its corporate wrongdoing but also for the flagrant personal excesses of the parties involved in the fraud. Both Kozlowski and Swartz were convicted on 22 theft and fraud-related charges, each earning a maximum term of 25 years in prison (Kemmerer & Shawver, 2011).

It seems from a traditional viewpoint that a startling lack of values and ethics had brought about this end. According to Kemmerer and Shawver (2011), this was not an isolated occurrence or a closed event and it is doubtful whether these dishonest actions can be attributed to an unethical or immoral organisation. Rather, it was a representation of the prevalent social norms that have influenced individuals within an enterprise in today's business world (Kemmerer & Shawver, 2011).

3.2.2.5 Arthur Anderson (2002)

In 2001, Arthur Andersen had more than $9 billion in revenue, with a reputation for outstanding audit results and expertise (Squires, Smith, McDougall & Yeack, 2003). At the time of the Enron failure, Arthur Andersen was Enron's official auditor (Hopkins, 2016). The company provided both audit and non-audit services to Enron, thus creating a possible conflict of interest. For example, the audit portion of Arthur Andersen would be reluctant to challenge Enron's management, as it would mean losing not only the audit services but also the lucrative non-audit services (such as management consulting). The company of Arthur Andersen had received $25 million for Enron audit services in 2001 and $27 million for non-audit services (Squires et al., 2003).

Arthur Andersen was indicted on one count of obstruction of justice linked to Enron in March 2002. The prosecution was the result of an investigation in which Andersen allegedly shredded work papers linked to the Enron scandal (Hopkins, 2016; Squires et al., 2003). The repercussions on Arthur Andersen were grave (Squires et al., 2003) and the company was convicted and decided to stop providing audit services to publicly traded companies (Hopkins, 2016). Public corporations lost trust in Arthur Andersen and moved to other accounting firms for their audit services. The audit branch of Arthur Andersen eventually folded, while the management consulting division was rebranded as Accenture (Squires et al., 2003). Wearing (2005) explains that by the end of 2002, Arthur Andersen as an audit firm was essentially finished, with a decline in its workforce from 85,000 to 3,000 and a barrier to auditing in the USA (Wearing, 2005).

The dissolution of Arthur Andersen served as a wake-up call and a turning point within the auditing community. Although Enron and Arthur Andersen were penalised, the public was not satisfied. The lack of corporate governance at Arthur Andersen was an obvious contributor to the corporate failures it was involved in.

3.2.2.6 Lehman Brothers (2008)

Lehman Brothers was founded in 1844, in Montgomery, Alabama, by German immigrant Henry Lehman. The company became known as Lehman Brothers, after Henry's brothers Emanuel and Mayer, joined him in 1850. In 1994, under the leadership of CEO Richard Fuld, the investment firm started to broaden its offerings. In the newly deregulated financial market, Lehman Brothers expanded its involvement in property dealing (or dealing with the company's own capital to make a profit for itself), securitisation, derivatives, wealth management and real estate. Lehman and other Wall Street companies were deeply involved in collateral debt obligations (CDOs) and mortgage-backed securities (MBSs) during the housing bubble of the early to mid-2000s. Between 2003 and 2004, Lehman also expanded into loan origination, acquiring five mortgage lenders, including those specialising in subprime mortgages, which were offered to weaker-loan borrowers who would not usually be able to secure a mortgage. In mid-2006, when house prices started to drop steadily, many subprime borrowers started defaulting on their payments, exposing the risky existence of these debts. Despite these warning signs, after housing prices declined, Lehman Brothers managed to produce subprime mortgages and expand its real estate holdings and by the end of fiscal year 2007, the company owned some $111 billion in commercial or residential real estate-related assets and securities (more than double what it owned at the end of the previous year). As investors and rating agencies expressed serious doubts about these types of assets due to their lack of liquidity on the market, they started to lose trust in Lehman Brothers and its investment banking peers because of the weakening of the real estate market. The first to go under was Bear Stearns, one of Lehman's closest rivals. This firm narrowly escaped bankruptcy with a sale to J.P. Morgan in March 2008. Rumours circulated after Bear's sudden collapse that Lehman Brothers would be the next to fall (History.Com Editors, 2018).

Lehman Brothers filed a bankruptcy petition in September 2008. It was the biggest insolvency procedure in the history of the USA. The 164-year-old company was the fourth largest USA investment bank and the global financial crisis prompted its bankruptcy (Amadeo, 2020). The USA economy faced the subprime mortgage crisis in 2007, which ultimately resulted in the fall of Lehman Brothers in 2008. The global recession was finally triggered by the effects of the USA subprime crisis (Foong, Ganesan, Pitchay, Haron & Hendayani; 2011).

Thus, Lehman Brothers, one of the biggest USA banks (Foong et al., 2011), collapsed in 2008. Their bankruptcy exposed the use of a mechanism known as 'Repo 105' to transfer off-balance sheet assets and debt to make their financial condition appear more attractive to investors. This indicated that they remained within USA GAAP limits, but still potentially misled investors (Hail, Tahoun & Wang, 2017). During the crisis, both of these operations raised confusion about the capital position of the major banks and investment firms (Koniak, Cohen, Dana & Ross, 2010). The SEC (2005) and Hail, Tahoun and Wang (2017) also support this, arguing that during 2010, the investigation of the Lehman Brothers bankruptcy by the court examiner revealed that off-balance sheet instruments were used fraudulently, as Lehman used a mechanism called Repo 105 to allegedly transfer assets and debt off-balance sheet to make its financial status more attractive to investors. The bank repeatedly participated in and listed short-term repurchase agreements as sales transactions. To convey the illusion of lower leverage to its buyers, it then used the sales proceeds to pay down debt. Lehman Brothers' auditors attested that the transactions conformed to GAAP (Hail et al., 2017).

According to Yu and Rudge (2014), as was the case with Lehman Brothers, a weak board can cause failure, despite a strong CEO. It was also the lack of independence of the auditors that led to the audit failure in the Lehman Brothers case. At that moment, their auditors were EY (di Fabrizio, 2016).

EY served as an independent auditor for Lehman Brothers from 2001 until Lehman filed for bankruptcy in 2008. It checked and signed-off on Lehman's financial statements during this time, giving the preferred unqualified opinion in each case. Anton Valukas, the Lehman bankruptcy examiner, raised serious questions about some of Lehman's accounting practices and the role EY played in enabling those things to remain unchallenged and concealed in its financial statements, in particular its use of and accounting for Repo 105 repurchase agreements, which allowed Lehman to move up to $ 50 billion from its quarter-end balance sheets. Valukas argued that the comments made by Lehman were deceptive and that there were credible allegations against EY for negligence and misuse (Wiggins et al., 2015).

EY contended that no wrong had been done. It was its view that Lehman's financial statements were prepared in compliance with GAAP and that no accounting problems had triggered Lehman's bankruptcy (Wiggins et al., 2015). As Lehman's Senior Vice President, Matthew Lee's duties included consolidating Lehman's subsidiaries' financial and accounting details from around the world into a single consolidated financial statement used by the organisation as the basis for its public reporting. On 16 May 2008, Lee sent a letter alleging accounting errors and other irregularities to several senior Lehman officers. Lehman's management sent the letter to its audit committee, which was requested to be aware of all the allegations made by Lee and to EY, which was directed to investigate the allegations. On 12 June 2008, William Schlich, the EY engagement partner, interviewed Matthew Lee at a meeting at which Lee also told EY about Lehman's growing use of Repo 105 and its effect on the balance sheet of the company. Lehman management and Schlich met with the audit committee of the Lehman Board in June 2008 to review the company's second quarter financial results. On 2 July 2008, Schlich met again to discuss the final statements with the audit committee. On 10 July, despite the Whistle-blower Document, EY released an unqualified report for the second quarter. Schlich attended a full board meeting on 22 July 2008 at which a Lehman officer gave a presentation on the Whistle-blower Letter. The presentation did not discuss the use of Repo 105. Notwithstanding its legislative responsibilities under SOX and the request by the audit committee to be aware of all the allegations made by Lee, EY did not notify the audit committee or the full board at any of those meetings of Lee's allegations concerning Repo 105. Anton Valukas argued that incompetence and malpractice amounted to such a mistake (Wiggins et al., 2015).

3.2.2.7 Madoff (2008)

The $65 trillion Madoff Dollar Ponzi scheme had been destroying the global economy. Questions were presented, such as "Why weren't the suggestions and allegations made by the investigated 'whistle blowers' years before the 'crash'?" (Quigley & Williams, 2013).

Bernie Madoff was very imaginative and saw the future of finance being done exclusively by robots and less and less through face-to-face contact. He was devoted to the digital future that sustained his rise on Wall Street (Quigley & Williams, 2013). According to the FBI, from at least 1980 until his arrest on 11 December 2008, Madoff carried out a scheme of defrauding clients by soliciting billions of dollars of funds under false pretences, failing to pledge investor funds and misappropriating and transferring investor funds for Madoff's own benefit and for the benefit of others without the investors' knowledge or permission (FBI, 2009).

Exactly when Madoff's Ponzi scheme started is not known. He testified in court that it began in 1991, but his account manager, Frank DiPascali, who had worked at the company since 1975, said that for as long as he knew, the scam had existed. Bernie Madoff made huge returns on investments, in ways that no other broker firm could (Quigley & Williams, 2013).

Several people tried to voice their doubts and suspicions about Madoff before Madoff's actual collapse. One such person was Harry Markopolos, a Rampart Investment Management portfolio manager in Boston. In 2000, Markopolos expressed concerns about the Madoff scam (Henriques, 2011). He said that if the press or officials of the SEC had taken an interest in his grievances and investigated the charges, Madoff would have been stopped in 2006 and saved billions (Chew, 2009). Michael Ocrant also tried to express his concerns and, in May 2001, he wrote an article entitled “Madoff tops charts; critics wonder how”. This article was published. He said that many of those who know Madoff in the hedge fund world were puzzled by the way the business had generated such consistent non-volatile returns month after month and year after year (Ocrant, 2001). Madoff’s tactics were criticised by so many analysts and individuals in financial circles, but no one was able to define precisely what was going on (Quigley & Williams, 2013). Notwithstanding those attempts, Madoff maintained the scam until 2008.

Investors gradually started wanting their capital. Madoff confessed to his son in December 2008 that he was struggling to collect $7 billion to cover redemptions (Henriques, 2008). Madoff proposed on 10 December that the organisation should allow bonus pay-outs. His sons confronted him and Madoff told them that they should continue the discussion away from the office at his house. Madoff admitted in the early hours of the morning that his company was a huge lie, and essentially, a giant Ponzi scheme. Madoff told his sons that nothing was left and he was completely preparing to go to prison (Henriques, 2008). On 11 December Madoff was apprehended by the FBI (Quigley & Williams, 2013),

Bernie Madoff was charged with 11 counts of criminal offences, including securities fraud, investment consultant fraud, mail fraud, wire fraud, international money laundering to facilitate specified unlawful activity, international money laundering to hide and mask the proceeds of specified unlawful activity, false perjury claims, false filing with the SEC and theft from an Employee Benefit Plan (Quigley & Williams, 2013). He pleaded guilty and was convicted in June 2009 by Federal District Judge Denny Chin. Judge Chin found the crimes of Madoff extraordinarily cruel and sentenced Madoff to a maximum of 150 years for his crimes (Quigley & Williams, 2013).

Many asked why the auditors had not raised concerns. David Friehling of Friehling & Horowitz, CPAs was excluded from his membership of the American Institute of Certified Public Accountants (AICPA) and the New York State Society of CPAs on 18 March 2009 following an ethics review. On the same day, the SEC lodged charges against F&H for false certification of having prepared the audit statements of broker-dealer company Bernard Madoff in accordance with GAAP. F&H was charged with misleading investors and faced a maximum term of 105 years in prison. The SEC further alleged that, as required under GAAP and GAAS standards, F&H failed to test the internal controls and did not maintain professional independence (Quigley & Williams, 2013).

Madoff’s attorneys demanded that Madoff be released early from prison in February 2020, arguing that he had a terminal kidney disease that could kill him within 18 months. Madoff is 10 years out from his 150-year sentence.

3.2.2.8 American International Group (AIG) (2008)

AIG rapidly expanded to become the world’s largest insurance company, reaching a $213 billion peak market capitalisation in 2001. AIG’s combined assets were $1,072 trillion at the end of the third quarter of 2007 and shareholder equity was $104.07 trillion. It was the world’s 18th largest public corporation in early 2008. It had raised annual losses of nearly $100 billion less than a year later and was rescued by the USA government with a $182.5 billion credit facility, meaning it had been essentially nationalised (Fatahi, 2017).

AIG was a global insurance company headquartered in the USA. In 2008, AIG was bailed out by the USA Federal Reserve. From 1999 to 2005, AIG was involved in a wide-ranging accounting scam that resulted in a $3.9 billion restatement in May 2005, which included various forms of transactions and claims related to a $500 million. In addition, AIG paid insurance brokers tens of millions of dollars in secret contingent commissions and engaged with insurance brokers and certain insurance firms in a bid-rigging scheme to split the market for certain forms of insurances.

The chairman, Hank Greenberg, and Joseph Cassano, who led the financial products subsidiary of AIG, were among the many people who lost their jobs and reputations. In an already highly competitive climate, AIG’s shortcomings stemmed primarily from risk blindness and the overarching desire to expand the business and its profits by 15% per annum. New York Attorney General, Eliot Spitzer, accused the firm of bid-rigging by insurance agents although nothing was ever proved against AIG. One severe accusation was substantiated, however; AIG created misleading accounts and used spurious reinsurance policies to inflate profits (Fatahi, 2017).

In its 2007 audit report for AIG, PwC noted a material weakness in internal control over financial statements related to the AIG super senior credit default swap portfolio valuation process and its supervision with respect to internal control concerns rather than valuation problems. The auditor’s remarks influenced the market, as investors started to doubt the company's level of exposure to the USA housing market, with AIG's share price dropping by 11.7% in one day. After significant write-downs of its credit default holdings in mid-September 2008, the USA Federal Reserve issued AIG with an $85 billion dollar loan to avoid its chaotic collapse and further crises on the financial markets (Woods et al., 2009).

One executive went to prison, the company paid $1.6 billion to resolve civil charges and Greenberg paid $15 million to settle charges from the USA regulator's SEC for manipulating AIG's documents to improve performance from 2000 through 2005. The resulting drop in the share price and decreased security ratings were a blow to the operation of the company's financial products in London. As the AAA rating vanished and posting cash collateral for its derivative products became more costly, the company ended up destroying its profit. The subprime crisis eventually ruined the portfolio of AIG's credit default swap. A seemingly risk-free stream of wealth turned into a liability of unprecedented proportions, almost overnight. This was a textbook example of risk blindness arising from a desire to seek profit at any expense (Fatahi, 2017). AIG settled for almost a billion dollars and PwC, the auditor, settled for $97.5 million to help the fraud (Lessambo, 2018).

3.2.2.9 General Electric (GE) (2018)

There is very limited literature available on the GE case, as this is still a relatively new case and the investigation is still in progress. In 2018, the American industry experienced the biggest annual stock decline of the modern period. Investors were blindsided against earnings by several multi-billion-dollar charges (Rausch, Onaran & Smith, 2019).

GE is a household name and has been around for decades since it was founded by Thomas Edison in the 19th century. The resulting stock slide wiped out more than half a trillion dollars in shareholder value since CEO Jack Welch developed GE into a banking giant with a peak market value of $594 billion in 2000, from less than $15 billion when he began in 1981. As of mid-January 2019, the drastic downturn under former CEO Jeffrey Immelt continued under John Flannery and now new CEO Larry Culp, reducing the market cap to $75 billion. The net leverage of the group, the debt as a multiple of a calculation of earnings, had almost doubled over the same time (Rausch et al., 2019).

A declining demand for energy-related goods such as gas turbines and equipment for oilfields reduced the prospect of a turnaround. Warren Buffett's Berkshire Hathaway holding company, which bailed GE out in 2008 through a $3 billion investment, sold GE shares worth $315 million.

GE's new blow came when accounting executive, Harry Markopolos, was charged with fraud for covering up $38 million, worth 40% of its market value. Markopolos said that to cover up its huge debts, GE had made false financial filings. Markopolos was allegedly working with an unidentified hedge fund, betting that the price of GE shares would fall. Markopolos maintained that GE was a bigger scam than Enron (de Luce, 2019).

Deloitte was hired by GE as their new auditors in 2020. The announcement marked the end of a centuries-old partnership that dated back to 1909 between GE and KPMG. In early 2018, GE announced that after a $6.2 billion loss in 2017 resulting from its GE Capital insurance portfolio, the SEC was investigating the company's accounting practices. GE said the SEC extended its inquiry in October 2018 after the firm took a $22 billion impairment charge on goodwill, much of which stemmed from the purchase of Alstom's power and grid sector in France in 2015. In May, 701 million shareholders, or 10.8% of the total votes cast, called on the GE audit committee to replace KPMG as the independent auditor of the company for 2020 (Brasseur, 2020). Once again, the lack of independence at KPMG may have led to GE's corporate failure and audit failure.

Summative comment on USA corporate failures

The McKesson & Robbins corporate failure of 1937 had a profound effect on auditing standards, leading to scrutiny and criticism of the accounting profession. It was found that there was unpaid inventory worth $21 million. The owner of McKesson & Robbins committed suicide in 1938. The auditors PriceWaterhouse did not perform the audits with the diligence expected from auditors and they repaid the audit fees to McKesson & Robbins. Enron was most probably one of the corporate failures which received the most media attention. Enron filed for bankruptcy in 2001. It was found that some assets and liabilities were kept off the balance sheet. This corporate failure resulted in convictions against the audit firm. Their auditors, Arthur Andersen, destroyed evidence that could have disclosed what had really happened at Enron. Arthur Andersen later shut its doors. This corporate failure was followed by WorldCom in 2002. WorldCom overstated its profits by more than $3.8 billion in 2001 and the first quarter of 2002. This corporate failure was not simply a case of accounting fraud, but reflected poor ethical leadership. Their auditors were also Arthur Andersen. This failure was followed by Tyco, the multinational manufacturing company. Tyco's management stole $150 million from illegal stock sales. The lack of corporate governance also contributed to this failure. In 2002, Arthur Andersen was indicted on one count of obstruction of justice linked to Enron and they decided to stop providing audit services to publicly traded companies. The audit branch of Arthur Andersen eventually folded, while the management consulting division was rebranded as Accenture. The lack of corporate governance at Arthur Andersen was an obvious contributor to the corporate failures it was involved in. In 2008 there were many corporate failures such as Lehman Brothers, AIG and Madoff. Lehman Brothers were exposed for their use of the Repo 105 mechanism to transfer off-balance sheet assets and debt to make their financial condition appear more attractive to investors. Their auditors, EY, were accused for not challenging and concealing its financial statements. Madoff's Ponzi scheme destroyed the global economy. The auditor, David Friehling of F&H, was charged with misleading investors and faced 105 years in prison. AIG, the world's largest insurance company's share price started to drop when their auditors noted material weaknesses in internal controls. AIG settled for almost a billion dollars while PwC settled for $97.5 million. In 2018, the household name, GE, made headlines when an inquiry was launched by the SEC into its accounting practices. The investigation is still ongoing. As can be seen above, the auditor practiced poor corporate governance, which then contributed to the corporate failures.

3.2.3 Corporate failures in Australia

The state of corporate governance in Australia has received media attention as the social and financial implications of major corporate collapses came to light. Most prominent in the local financial press have been the investigations of governance irregularities (and allegations of illegal management behaviour) at HIH and One.Tel, with supporting roles from companies such as Harris Scarfe (Fleming, 2003). Some of these high-profile corporate failures in Australia are discussed below.

3.2.3.1 HIH insurance (2001)

According to du Plessis (2003), HIH was the worst corporate failure in Australia's history.

HIH included a variety of insurance firms and became Australia's biggest underwriter of insurance. The failure had far-reaching consequences, as HIH was a major provider of all forms of insurance in Australia, including most public risk coverage. HIH was seen as a price cutter and a more aggressive underwriter than its rivals in the insurance industry (Brown, 2001). An ex-director, Rodney Adler, claimed that excessive discounting was one of the factors that led to the failure of the company (Gaylord 2001). Nevertheless, without proper due diligence investigations, it was undoubtedly the hostile takeover for AUD$300 million of FAI Insurance, a large Australian insurance firm, that marked the beginning of the end for HIH. Ray Williams, the founder and CEO of HIH, acknowledged that the price paid for the takeover was too high (Brown, 2001). HIH also suffered major losses in its operations in the US and UK, which contributed to its eventual demise.

By 27 August 2001, when the company was wound up, the deficit was projected to be between AUD$3.6 billion and AUD$5.3 billion (Allan, 2006). The case of HIH was also unquestionably an auditing failure (Allan, 2006), reflecting poor corporate governance at Arthur Andersen, HIH's auditors. Arthur Andersen audited HIH from 1971 until the company was partially liquidated in March 2001 (Kehl, 2001). During this time Arthur Andersen developed a professional relationship with HIH (Mirshekary et al., 2005). Andersen's integrity was extremely doubtful (Allan, 2006) and their independence was questioned, especially its relationship with HIH senior management (Mirshekary et al., 2005). The audit firm's three former partners sat on the board of HIH. One of the partners, who was the beneficiary of Andersen's continuing benefits, was made president and nominated to the audit committee just 17 months after his retirement. The day after his departure from the firm, another partner, who had been the engagement partner, was made CFO of HIH. Just five months after his retirement, the third was appointed to the board, having played a major role in HIH's audit for 25 years (Allan, 2006). All three of these men were well-known to the current partners and employees of Arthur Andersen, as they held roles that considerably dominated the financial affairs of HIH (Mirshekary et al., 2005). There is evidence to suggest that the independence of Andersen was also in doubt due to the high-pressure relationship between HIH executives and Andersen's audit team. Since HIH management refused to increase audit fees for Arthur Andersen, Arthur Andersen decided to reduce the amount of work that had been performed on the HIH audit (Mirshekary et al., 2005).

In addition, Arthur Andersen's long-time HIH audit partnership partner was replaced in 1999 after consulting with non-executive directors in the absence of senior managers. The Commission claimed that due to Andersen's strong personal association with HIH and Andersen's unquestioned approval of the findings of both the internal audit processes of the HIH and the consultancy work, Andersen was not impartial in performing the 1999 and 2000 audits (Allan, 2006).

The HIH corporate failure highlights the lack of independence of the auditors and how this contributed to the failure of HIH (Correy, 2001; Mirshekary et al., 2005).

3.2.3.2 Harris Scarfe (2001)

Harris Scarfe represents one of the biggest corporate failures in Australia, with $265 million in debt. The consequences of this crisis certainly had a negative impact on the accounting profession and on the Australian auditing industry (Kavrar & Yilmaz, 2017).

The retailer Harris Scarfe had been in business for 150 years before it was placed under voluntary administration by the directors on 2 April 2001. This occurred after irregularities were found dating back six years. The company was placed in receivership. In their report to creditors, the administrators pointed out that the systemic benefit overstatement was funded by increased debt, both to the bank and to creditors (Peacock, 2001). After investigations by ASIC and official audits by the company's receivers and managers, ASIC claimed that the CFO, Alan Hodgson, had altered Harris Scarfe's accounts to inflate the company's profits. In reality, it was found that Hodgson had played a leading role in falsifying accounts and records and creating a false image that Harris Scarfe was in good financial health, enabling it to trade when it was practically insolvent (Leung & Cooper, 2003). In a testimony given to the South Australian Supreme Court, Hodgson told the court that, if the company's managing director or chairman asked for a particular profit result, he effectively allowed accounts to be changed (Tabakoff, 2001). Hodgson was sentenced to serve six years in prison (Leung & Cooper, 2003).

ANZ bank filed a lawsuit against the auditors of Harris Scarf, EY and PwC, demanding reimbursement of at least AUD$70 million and alleging that the auditors were inept in failing to identify the accounting anomalies and fraudulent entries in the management accounts. A plaintiff also brought a class action against the management, alleging they have committed fraudulent, deceptive and misleading acts over a five-year period. As a result of the false statements, the shareholders argued that investors paid more than the true market value of the stock and ultimately lost the ability to sell their stock (Wood, 2002).

In Harris Scarfe's fall, it seems the accountants were running two sets of books which were not picked up by the auditors. The board's audit committee also had independence problems. The company had an audit committee of three members, two of whom were clearly internal (including Hodgson) and one of whom was technically autonomous, meeting only twice a year. An audit committee should be an independent body in order to ensure effective and successful collaboration between external auditors and the senior management. Clearly, this did not work (Correy, 2001). Nevertheless, the principal creditor, ANZ bank, sued the auditors for many years, citing negligence in not reporting the discrepancies. According to Kavrar and Yilmaz (2017) the most unethical issues came from the management of Harris Scarfe and from the accounting firms, EY and PwC.

3.2.3.3 One.Tel (2002)

One.Tel, an Australian telecommunications firm, was put in bankruptcy and then liquidated in May 2001, with a total debt of AUD$600 million. The joint managing directors, Jodee Rich and Brad Keeling, had each received bonuses of AUD$7 million the year before One.Tel revealed a loss of AUD$291 million. The bonuses totalling AUD$14 million were paid in 1999, but the benefits were treated as accrued expenditures by a change in accounting policy and viewed as set-up costs associated with One.Tel companies in Europe and Australia. At one point, when the company owed AUD$33 million in bills, the bank had only $500,000 and the liquidity issue was not reported in a management report to the directors at that time (Leung & Cooper, 2003).

During an investigation on One.Tel, it was found that questionable accounting practices successfully concealed multi-million payments to Jodee Rich and Brad Keeling (Hughes, 2002; Leung & Cooper, 2003). Along with other questionable 'improvements' in accounting, this practice had the effect of transforming a loss into revenue. The auditors allegedly supported the questionable accounting (ABC Newsonline, 2002).

3.2.3.4 Dick Smith Electronics (2016)

Dick Smith Holdings (formerly Dick Smith, Dick Smith Electronics or DSE) was an Australian retail chain that marketed consumer electronics products, electronic parts for hobbyists and electronic project kits for retail stores. The chain successfully spread to New Zealand, but was not successful in many other nations. Dick Smith founded the company in Sydney in 1968 and owned it together with his wife until they sold 60% to Woolworths in 1980 and the remaining 40% two years later. The firm closed in 2016, four years after Anchorage Capital Partners purchased it (Wikipedia, 2020).

Dick Smith Holdings shocked the market on 30 November 2015 by revealing that it needed an inventory write-down of AUD$60 million, although the company's financial statements for 28 June 2015 were audited three months earlier with no adverse findings. Inventory management is the core of a retail company and can be seen by auditors as a main risk area. Therefore, the issue of inventory either existed over a short period of time or it grew over a longer period of time and was overlooked by the auditors (Gray, 2016).

Dick Smith announced on 5 January 2016 that it had selected receivers and administrators. Customers who had bought Christmas gift cards in 2015 were told that they would not be honoured. The timing of the receivership was decided by the banks of Dick Smith as they ranked above other creditors (Gray, 2016).

Shareholder action was taken against former CEO, Nick Abboud and ex-CFO Michael Potts. They were accused that Dick Smith's management did not properly account for its inventory, especially house brand goods that executives such as former Marketing Director, Neil Merola, said were stacking up in their warehouses when they did not sell. At the time, ChannelNews announced that the retailer had been supplying batteries for three years. Between June 2013 and June 2015, inventories at the retailer rose from AUD$171 million to AUD$293 million. In late 2015, Dick Smith wrote off AUD$60 million of inventory. The former directors were accused of not providing an accurate and realistic view of their financial situation in the 2013, 2014 and 2015 financial years as a consequence of failures to report details in their financial statements (Richards, 2019).

Dick Smith's auditors had been Deloitte. The audit firm was drawn into the legal battle between the beneficiaries, Dick Smith and their former directors (Spencer, 2015). Two years after one of Australia's greatest consumer electronics retail disasters, Deloitte were still seeking to remove themselves from the AUD$400 million failure, with limited success. Deloitte was ordered by the New South Wales (NSW) Supreme Court, Justice Michael Ball, to submit an additional laptop containing data from its audits after failing to strike out complaints which were brought in by two shareholders, claiming that the company's accounting work on the retailer was negligent (Richards, 2019).

The order for the laptop was released on 24 April and it came after the court ruled against the company's request to strike out the allegations. It was argued that if the financial statements of Dick Smith had been revised or a qualified audit opinion had been given in favour of them, Dick Smith would not have floated and been listed on the ASX. The NSW Court was told that the failure of Deloitte to detect these inventory problems during the company's audits meant that Deloitte failed to perform its audits in compliance with the auditing standards necessary and that they did not exercise fair expertise and care and were engaged in misleading and deceptive activity. There were two more lawsuits against the bankrupt retailer, one against Abboud and Potts and non-executive directors, and another against Abboud and Potts by NAB and HSBC. In February 2020, the four claims were expected to be heard together. The defendants had already lodged cross-claims against Deloitte in each of the four cases (Richards, 2019). The case is still in progress.

Summative comment on Australian corporate failures

The failure of HIH, an insurance underwriter, was the worst corporate failure in Australia. Their aggressive discounting was one of the factors that led to their failure. Poor corporate governance contributed to the failure of HIH. There were independence issues between HIH and their auditors, Arthur Andersen. This was followed by the failure of Harris Scarfe in 2001. It was found that the CFO falsified accounts and records, creating the impression that Harris Scarfe was in a sound financial position. The most unethical issues came from the management of Harris Scarfe and from the accounting firms EY and PwC. The telecommunications company, One.Tel, was liquidated in 2001. Their questionable accounting practices led to their failure, supported by their auditors. In 2016, Dick Smith Electronics revealed that AUD$60 million of inventory had to be written down. The former directors were accused of not providing an accurate and realistic view of their financial position in the 2013, 2014 and 2015 financial years. It is suspected that their auditors, Deloitte, did not perform their audits in compliance with the auditing standards.

3.2.4 Corporate failures in the Netherlands

The Royal Ahold failure was a high-profile accounting and auditing scandal in Europe (Knapp & Knapp, 2007). Even though there might have been smaller insignificant corporate failures in the Netherlands, Royal Ahold received the most media attention, as discussed below.

3.2.4.1 Royal Ahold (2003)

According to de Jong et al. (2007), the rise and fall of Royal Ahold (Koninklijke Ahold NV) was a major event. With its headquarters in the Netherlands, Ahold was one of the largest multinational food service and supermarket store firms in the world. Revenue and profits registered at their peak in 2001 with €66.6 billion and €1.1 billion, respectively and it operated 5,155 stores in 27 countries with almost a quarter of a million employees. Ahold started out as a family business in 1887 and went public in 1948. Under the Heijn family, the company was a family-controlled business, based mainly in the Netherlands for more than 100 years. Ahold underwent a transition from a family-controlled company to a management-controlled company in 1989. The company witnessed a remarkable period of success after the transition. It produced a return of over 1,000% for its shareholders and had a €30.6 billion market capitalisation by November 2001. Yet Ahold experienced a complete breakdown in February 2003, with shareholders having lost most of their produced returns since 1989. The era that followed saw a company in complete disarray: a botched plan, an accounting scandal and professional management dismissal and lawsuits from all parts of the world. The dispute involved the $1.1 billion settlement between the corporation itself and its USA creditors, the fifth largest settlement in the USA and the largest involving a USA foreign corporation (Bickerton, 2005). Ahold was branded 'the Enron of Europe' (The Economist, 2003; Benston & Hartgraves, 2002).

In 2000, the Dutch company Royal Ahold, acquired Food Service. USA Food Service was the second-largest food distributor to restaurants, hotels, colleges, hospitals and the vast USA grocery stores chains of Ahold. A part of USA Food Service's balance sheet was vendor-receivable promotional allowances (seller rebates). As part of the regular USA audit procedures, Deloitte, independent auditors of Ahold, sent confirmations for those receivables. Confirmations were sent to sellers and returned without exception. The auditors gave unqualified reports for the first two years after the acquisition. Nevertheless, during the 2002 audit, independent auditors of Ahold noticed problems and immediately revoked their audit opinions for 2000 and 2001 and postponed their 2002 audit (Masters & McCartney, 2003). Ahold announced on 24 February 2003 that it would restate earnings downward for fiscal years 2000 and 2001 and by a combined total of at least $500 million for the first three quarters of 2002 and that a forensic accounting investigation would be launched, mostly due to irregularities at Ahold's subsidiary, USA Alimentary service (Sanchez & Agoglia, 2011).

Jong et al. (2007) state that in 2002, Ahold had not reported major off-balance sheet commitments related to some of its joint ventures and recorded a second quarterly loss for the year by the third quarter. The chairman of the supervisory board announced on 23 February 2003 that earnings for 2002 would be slightly lower than previously reported. Inflated USA Foodservice vendor rebates had theoretically overstated €466 million in earnings. Eventually, over the three-year period 2000–2002, the amount was €820 million. Therefore, Ahold's financial statements could not have merged four existing, and one former joint project. It was later announced that CEO, Cees van der Hoeven, and CFO, Michael Meurs, had resigned. The markets replied to the announcement with an unprecedented 59.4% return on the stock market and a 27.4% to 28.3% decline in Ahold's bond prices.

The supervisory board had struggled to adjust to a professionally run company with a decentralised system of ownership. The OECD supervisory board structure and duties suggest that the problems reported for Ahold were mainly the responsibility of the board. The members of the supervisory board must be professional and willing to commit adequate time to the company (John & Senbet, 1998). The supervisory board is particularly relevant in the Netherlands, where after 2001 main voting rights of shareholders were transferred to the supervisory board either by Dutch law or by company laws as in the case of Ahold. Thanks to the involvement of former executives and subordinates with competing interests with other stakeholders, Ahold's supervisory board was not neutral (de Jong et al, 2007).

Several members of the board had ties to Ahold-related institutions, which led to conflicts of interest with these stakeholders. Nelissen, a board member from 1987 to 2001, was the CEO of Amsterdamsche en Rotterdamsche Bank (Amro), one of the main banks of Ahold. When Amro and Algemene Bank Nederland (ABN) combined in 1990, Nelissen was the combination's CEO until he retired in 1992. After the retirement he became a supervisory board member of the bank. Ahold had interlocked directorates with two other Dutch financial institutions, Nationale Investeringsbank and ING (a Dutch multinational banking and financial services corporation headquartered in Amsterdam), via Kreiken and Choufoer (members of the supervisory board). Choufoer was also from Royal Dutch Shell, a 15-year-old employer for van der Hoeven. Sir Perry was Unilever's former CEO, an important consumer goods supplier to Ahold (de Jong et al., 2007).

PwC's independent report noted Ahold's inadequate corporate controls and questionable financial and accounting practices. A total of 275 accounting violations out of 470 were attributed to insufficient internal controls. The forensic audit also revealed that there was a lack of information about the Dutch GAAP and USA GAAP in Ahold and the implications of the actions of the management as more accurately reflected in the USA GAAP numbers. Deloitte & Touche, Ahold's auditor found the issues at an early stage of USA Foodservice. Around the time of purchase of USA Foodservice in 2000, Deloitte conducted a due diligence investigation. Deloitte suggested that the method used to monitor USA Foodservice vendor allowances was very opaque (Smit, 2004). As part of their 2002 year-end report, Deloitte also revealed the extent of Ahold's accounting irregularities (de Jong et al., 2007).

Ahold's policy and investor relationships, combined with its poor corporate governance, had a huge effect on the accounting practices of the companies and their fraud. Starting with the family and continuing under skilled management, all the protections available to Dutch companies were embraced by the family and management to gain and retain full control over Ahold. These overt manipulations of management's corporate governance by Ahold prevented shareholders from tracking day-to-day management and the market's ability to influence management for corporate control. This power helped management to overtake the supervisory board, which was the last institution that stood in the way of the firm's full control of management (de Jong et al., 2007).

This situation forced the Netherlands and European officials to question their approach to corporate governance and accounting policies. A corporate governance committee was established in the Netherlands on 10 March 2003 (Tabaksblat Committee) to restore trust in public companies. In the USA, the PCAOB used Ahold as an example for successfully negotiating the expansion of its supervision to European accounting firms operating in the USA or operating on international companies listed in the USA (Schroeder, 2003).

In the 1990s, Dutch efforts to improve governance were focused on self-regulation (de Jong et al., 2005). With regard to other self-regulating regions, the track record of corporate governance self-regulation was not promising (Coglianese, Keating, Michael & Healey, 2004). Since the dissolution of Ahold, the collection of standards and best practices of the Tabaksblat Committee has become a part of Dutch law, requiring companies to follow or justify their non-compliance. There is, however, no clear legal compliance or control, so defences to take over, such as certificates, are still valid. The Tabaksblat Committee assigns primary supervisory duty to shareholders; however, shareholder rights are not returned explicitly (de Jong et al., 2007).

Among other claims, the SEC alleged that the two auditors had relied on implausible representations made by company officials. In failing to examine such questionable statements and other clear red flags during the 1999 audit, the SEC concluded that the two auditors had failed to demonstrate a reasonable degree of professional caution and failed to recommend sufficient changes to the USA financial statements from Foodservice and failed to collect adequate qualified evidence to support their audit opinion. The SEC noted that the auditors had facts in their possession that could have prevented the fraud. Instead, since they failed to practice sufficient qualified cynicism, the fraud was allowed to proceed (Walker, 2006).

In 2003, independent auditors of Royal Ahold suspended their firm's fiscal 2002 audit after they found several possible anomalies in the accounting records of the company. The discovery of the huge accounting fraud resulted in criminal and civil litigation being filed in both Europe and the USA against the company and its top executives (Knapp & Knapp, 2007). Given the fact that the executives of the company knowingly misled Royal Ahold's auditors, Deloitte, and the fact that those auditors were eventually responsible for stopping the fraud, several parties assumed that Deloitte should have detected and reported the fraud earlier than it did. In reality, Deloitte had been named a defendant in many major class action lawsuits filed following the fraud's first published reports. Most are considered at least partly liable for the Royal Ahold fiasco by regulatory authorities and supervisory bodies within the accounting profession. Finally, several parties argued that a significant measure of blame for the audit failures involving multinational companies such as Royal Ahold and Parmalat should be collectively borne by the tiny fraternity of international accounting firms that dominate the global auditing discipline (Knapp & Knapp, 2007).

It should be noted that significant corporate failures in the Netherlands are considerably fewer than in other countries, which could be due to the fact that Dutch auditing firms apply the legislation, recommending that an independent supervisory board be appointed. The auditing firms' annual reports also disclose that they appoint a supervisory board which is fully independent from the auditing firm. This proves the importance of independence in corporate governance and auditing firms.

Summative comment on corporate failures in the Netherlands

Royal Ahold's rise and fall was a major event in the Netherlands. This company did not report major off-balance sheet commitments related to joint ventures. Several members of the board had ties with Ahold-related institutions which led to conflicts of interest with these stakeholders. The forensic audit also revealed that there was a lack of information about the Dutch GAAP and USA GAAP in Ahold and the implications of the actions of the management as more accurately reflected in the USA GAAP numbers. Deloitte found the issues at an early stage of USA Foodservice. Ahold's policy and investor relationships, combined with its poor corporate governance, had a profound effect on the accounting practices of the companies and their fraud. This forced the Netherlands and European officials to question their approach to corporate governance and accounting policies. Given the fact that the executives of the company knowingly misled Deloitte and the fact that those auditors were eventually responsible for stopping the fraud, several parties assumed that Deloitte should have detected and reported the fraud earlier than it did.

3.2.5 Corporate failures in South Africa

Prior to Steinhoff in 2017–2018, there were many other corporate scandals and failures in South Africa, such as LeisureNet, Regal Treasury Bank, Randgold & Exploration and Goldfields, to name only a few. According to Professor Wiseman Nkuhlu (2020), chairman of KPMG South Africa, corporate failures such as Steinhoff, Tongaat Hulett and VBS Bank happened because auditing firms are driven by revenue and profits and there is a lack of independence to provide effective oversight. The corporate failures in South Africa that received the most media attention in the recent years are discussed below.

3.2.5.1 Steinhoff (2017/2018)

Established in 1964, Steinhoff International Holdings NV (Steinhoff) was a South African company dealing primarily in furniture and household goods. Steinhoff suffered major setbacks in December 2017, when its share price plunged after an inquiry into accounting irregularities and its CEO, Markus Jooste resigned (Park, 2017).

Steinhoff released a statement in December 2017 on the Stock Exchange News Service (SENS) of the JSE, alleging that there were accounting irregularities requiring further investigation (Putzier, 2019). In January 2018, within a month of the disclosure, Steinhoff's market capitalisation decreased by $10 billion, flagging it as one of the greatest ever accounting scandals in South Africa (Cotterill, 2018b). Its market value plummeted by 80% following the announcement that Deloitte could no longer rely on its financial statements for 2015 and 2016, despite being signed off as unqualified (Putzier, 2019).

Markus Jooste and his associates sought to enrich themselves thus defrauding the company and its shareholders. They used a global network of businesses to do so, including tax havens such as the British Virgin Islands (Open Secrets, 2020). The auditors at the time, Deloitte, were also hesitant to give a final opinion on the consolidated financial statements. The following question was left unanswered: 'Why would Deloitte publish an unqualified auditors report for the financial statements of 2015/2016' (Niselow, 2018)? Since the corporate crisis involved an accounting mistake, the question remained whether Steinhoff had followed the King Report recommendations (Naude, Hamilton, Ungerer, Malan & de Klerk, 2018).

A forensic report by PwC found that a small group of former Steinhoff executives and other non-Steinhoff executives led by a senior executive, orchestrated and executed false and fraudulent transactions and misrepresented a profit of over R100 billion for at least a decade (Open Secrets, 2020).

The failure of corporate governance was disastrous, severely damaging the public interest. A total of 948 pension funds had been invested in. The company lost 98% of its value in just two years as a result of the fraud and much of this occurred in September 2017 within 24 hours. The Government Employees Pension Fund (GEPF), with accounts for retired civil servants alone, had lost more than R21 billion (Open Secrets, 2020).

Questions were raised why Deloitte had not identified any irregularities. From the time the Steinhoff listed in 1998, Deloitte had been the external auditor to the company. Deloitte reported that Steinhoff's financial statements "fairly reflected the financial condition of the company in all material respects" each year for 20 years. They were evidently unaware of the billion-rand void in the company's finances until 2017. It was too late, when they eventually declined to sign off the statements in November 2017 (Open Secrets, 2020).

Deloitte acknowledged the need for an inquiry by the IRBA in 2018, but said they remained confident in their conduct. Deloitte defended itself by stating that it flagged concerns about the 2017 accounts, but this was done only after a criminal investigation had started in Germany (Open Secrets, 2020).

Deloitte had been an auditor of Steinhoff for two decades. This kind of strengthened relationship ultimately compromises the independence an auditor can exercise. The long-running work which Deloitte had done with Steinhoff meant that Deloitte should have had much greater insight into the business and how it worked (Open Secrets, 2020).

In South Africa, Steinhoff is a recent example which exposed the gaps in the balance of power in the structure of the company. The position of auditors, as an autonomous body that should review records and check compliance with accounting processes, was at its core once again. Investigations found that top executives were purposely misrepresenting financial data (Maranga, 2018).

3.2.5.2 VBS Bank (2018)

The Steinhoff corporate failure was shortly followed by the VBS Mutual Bank scandal (Putzier, 2019). Sipho Malaba, lead auditor for KPMG in the VBS R1.8 billion scam, played an active part in covering up the fraud and was rewarded with R34 million. Malaba attempted to cover up the money he had obtained from VBS as loans, but his reasoning was rejected by the investigator. Malaba received significant facilities from VBS which were not disclosed to KPMG and could not be considered arm length borrowings. In cases where he believed the financial statements were misstated, he gave an unqualified audit opinion. He also gave an opinion on the regulatory audit which he knew was inaccurate (Ritchie, 2018). Had Malaba and KPMG blown the whistle, theft may have ended sooner (Cowan, 2018).

Both KMPG partners may be held responsible for a possible R1.89 billion lawsuit following its catastrophic VBS audit. Because KPMG is a company, anyone who was a partner with KPMG at the time of the audit would be responsible for the loss. An unnamed senior audit professional stated that the findings from the VBS scandal could spell the end of KPMG South Africa. He stated that dissolving the partnerships and finding new partners and new employees would be best for KPMG South Africa (de Wet & Wasserman, 2018).

KMPG took action when the matter came to light. Nkuhlu (2020) stressed that no behaviour that would compromise the quality and integrity of KPMG's work would be tolerated. He also said KPMG has made improvements to ensure it rebuilt confidence in KPMG among the public and clients (Ritchie, 2018).

3.2.5.3 Nkonki Inc. (2018)

Auditing firm Nkonki Inc announced it was going into voluntary liquidation after auditor general Kimi Makwetu stated that Nkonki and KPMG would no longer work for his office (Haffajee, 2018). According to Haffajee (2018), Salim Essa, who had links to the Gupta family, connived with a Nkonki partner to position Nkonki as an accomplice to the Gupta empire by giving its various questionable deals the stamp of auditor approval.

Most of Nkonki's work was in the public sector and therefore it would no longer be able to survive. About 180 staff were left without jobs (Haffajee, 2018; Institute of Certified Bookkeepers and Accountants, 2018). Nkonki's chief executive, Mitesh Patel, resigned after the investigative journalism unit, amaBhungane revealed that his R107 million 'management buyout' of Nkonki was funded by Essa (Comrie & Brümmer, 2018). Patel's 2016–2017 Gupta-funded purchase of roughly 82% of Nkonki from founders, Sindi Zilwa and her brother, Mzi Nkonki, was one of the latest scandals to undermine the increasingly discredited audit profession. Nkonki had become the freshest casualty of the Guptas' state-capture project, joining the ranks of KPMG and McKinsey (Institute of Certified Bookkeepers and Accountants, 2018).

According to amaBhungane, the intention was for Patel to hold 65% of the shares he bought as a front for his funders, ultimately Essa. After the transaction, Nkonki secured new work potentially worth hundreds of millions at Eskom, then under the sway of the Guptas. Patel denied this when confronted by amaBhungane but resigned on 9 April 2018. In a letter to staff, Patel said his resignation was 'amicable' and was reached in consultation with the firm's EXCO (Institute of Certified Bookkeepers and Accountants, 2018).

Thuto Masasa was appointed as acting CEO and Nkonki hired a law firm to conduct a forensic investigation of the firm. It was impossible for Nkonki to have conducted and obtained the outcome of a thorough forensic investigation into the serious allegations posed in the media prior to the auditor-general terminating its mandate with the company. The firm also did not have the opportunity to address the serious and damaging allegations in respect of Patel's shareholding in Nkonki. The company described its 180 employees as victims who had no involvement or knowledge in the shareholding and loan transactions, its funding or its due diligence processes (Institute of Certified Bookkeepers and Accountants, 2018).

The IRBA confirmed that an investigation letter was issued to Nkonki on 29 March 2018 due to concerns that there may have been contraventions of Sections 38 and 41 (6) (e) of the APA. These provisions sought to ensure auditor independence and required auditing firm shareholders to be directors and vice versa and ban the sharing of audit fees with non-auditors. The loan at Nkonki potentially put Nkonki on the wrong side of both.

From the events at Nkonki, the lack of corporate governance and unethical behaviour of the audit firm's directors was evident. It possible that the audit firm failure of Nkonki could have been avoided had the firm implemented proper corporate governance and had an independent oversight board.

3.2.5.4 KPMG (2017–2018)

Eight senior executives were sacked from KPMG South Africa in September 2017. This followed on from the scandal involving President Jacob Zuma and the Gupta family. The layoffs at KPMG came after an internal inquiry found that the accounting firm had been ignoring red flags in the auditing of Gupta family-owned businesses. KPMG issued alerts about the honesty and ethics of the Guptas but failed to act early enough on those alerts. In March 2016 the political crisis deepened when KPMG terminated its 15-year association with the Guptas (Shoaib, 2017). At the time, KPMG CEO, Trevor Hoole, acknowledged the company should have stopped working for Gupta companies earlier than they did. KPMG and Bell Pottinger were accused by a civil society group, Save South Africa, of playing a central role in facilitating state capture. Many South Africans have little faith in the independence of state security agencies and the national prosecutorial authority (Cotterill, 2017).

KPMG became central to the Gupta family controversy, as the leaked emails revealed that its South African office allowed Gupta-owned company, Linkway Trading, to consider spending on a Gupta family wedding in 2013 as a business expense. KPMG executive Moses Kgosana, referred in an email to the wedding as the 'Millennium Gathering'. Four KPMG partners also attended the wedding (Cotterill, 2017).

KPMG has also disavowed its research on a 2015 study used by state prosecutors to try to discredit Pravin Gordhan, a former finance minister and one of the toughest critics of the Guptas (Cotterill, 2017). KPMG stated it would pay an anti-corruption charity for the R40 million it received from auditing Gupta-owned companies since 2002. KPMG also paid back R23 million received from writing the 2015 report used to support allegations that Gordhan had set up a rogue tax surveillance unit when he headed the finances. KPMG said they would no longer rely on the report (Cotterill, 2017).

KPMG International performed an inquiry and, given the shortcomings in the audit work, they found that there was no proof of dishonesty or unethical actions by partners working on the Gupta audits. The auditing firm added that Gupta-linked company managers had reacted misleadingly and inadequately to KPMG's inquiries about the existence of related party relationships and the extent of significant irregular transactions in the sector. KPMG denied participation in or condonation of any suspected money laundering activities related to Gupta-owned firms or facilitation of offshore tax evasion (Cotterill, 2017).

Karthik Ramanna, professor of business and public policy at the Blavatnik School of Government at the University of Oxford, pointed out that KPMG had earlier ethical problems, including a 2005 dispute with the US government over illegal tax shelters (Cotterill, 2017). South African Reserve Bank governor, Lesetja Kganyago, stated that KPMG had to take responsibility for their actions. They had acknowledged research which they have never should have. He also stated that KPMG audited or co-audited four of South Africa's largest five banks and if they were to be fired by those banks, it would leave the country exposed, with only three auditing firms, which was not good for competition (Pilling, 2017).

The IRBA investigated the claims that KPMG and the Gupta family were involved. IRBA CEO Bernard Agulhas, said the inquiry would take place regardless of the fact that KPMG had ended its 15-year association with the Gupta family. He pointed out that the IRBA took these claims very seriously as it would have a huge impact on the public domain and the public interest (Crotty, 2017).

KPMG undermined the very core of corporate governance and the reputational credibility of the external audit, and had done so for a long time in the face of its clients' clear financial and company malpractice (Abedian, 2017). KPMG's actions had struck at the heart of corporate governance, according to Hlengiwe Zondo-Kabini, of corporate governance law firm Fasken Martineau. She stated that the executives' poor judgment had undermined their fiduciary duties. She also claimed that the executives of the auditing company as well as other parts of KPMG, such as advisory, were guilty of poor governance of the business. The reputation of KPMG was seriously affected and the entire processes and management of KPMG needed to be checked (Hosken, 2017).

KPMG strengthened its procedures in corporate governance. The company agreed to follow additional criteria as outlined in King IV and to nominate an INED to support the existing members of the board to restore public trust (KPMG, 2017). The question remains, why does it take corporate failures of this magnitude before corporate governance is taken seriously? Why have auditing firms waited so long to implement the King Code?

3.2.5.5 Tongaat Hulett (2019)

Tongaat Hulett released a SENS on 31 May 2019 stating that its analysis had uncovered past activities that were of serious concern to the board and the auditors of the firm (Tongaat Hulett, 2019). Clear references were made to past activities that appear to have contributed to financial statements that did not adequately represent the actual operating results of Tongaat Hulett (Tongaat Hulett, 2019) and were subject to ongoing independent forensic review (Putzier, 2019).

Senior executives at Tongaat Hulett, including the CEO of 15 years, Peter Staude, were suspected of making various misrepresentations in the financial statements. The alleged fraud ranged from misrepresenting the value of the assets, falsely reporting the expenditures as assets, claiming revenue from the sale of land that had not yet been sold and then failing to report it when some of those deals dropped. Tongaat reported in December 2019 that the 'unwanted' activities resulted in the 2018 financial statements being incorrect by nearly R12 billion and that the company's assets had been overestimated by R10 billion (Open Secrets, 2020).

This was supported by Business Insider SA (2020) and Stoddard (2020), who state that Tongaat Hulett disclosed that the equity (the value of the business after liabilities) in its 2018 financial results had been overstated by between R3.5 billion to R4.5 billion. The adjustments were of a non-cash nature and related to the reassessment of land sales against the revenue recognition criteria defined by International Financial Reporting Standards and the associated profit margins. Therefore, the equity on its balance sheet was cut by between R3.5 billion and R4.5 billion. Analysts believed its property portfolio, in particular, was inflated. An external report blamed 10 former executives, including ex-CEO Peter Staude, who was paid more than R170 million in a decade. Tongaat shares remain suspended on the JSE and in London (Business Insider SA, 2020).

Tongaat stated that once the forensic investigation and report findings are complete and the final accounting treatments are resolved by the company, the auditors will complete the outstanding audit processes (Stoddard, 2020). As this corporate failure is very recent and the investigation is still in progress, there is very little information available.

3.2.5.6 Eskom (2020)

South Africa's state power utility demanded that audit firm PwC repay it R95 million, alleging the money was disbursed under an invalid contract. PwC denied the allegation. PwC's 2017 contract to cut costs at Eskom was illegal, unconstitutional and thus null and void, stated Sikonathi Mantshantsha, the utility's spokesman. Eskom sent a letter of demand for the fees to be returned. An investigation Eskom commissioned from G9 Consulting and Advisory Services found that PwC took credit for work Eskom had done itself, according to the amaBhungane Centre for Investigative Journalism, which first reported the development. The probe also found the payment structure was unlawful. PwC said it won the Eskom contract after a competitive bidding process and that on average, 27 of its staff worked full-time for a year on the project, which identified potential savings of R56 billion for the utility. The quantum of fees referred to by Eskom in its letter of demand was for the entire project team, which included three other professional services firms (Burkhard, 2020).

PwC's own investigations to date did not identify any basis on which to accept Eskom's demand. While PwC cooperated with the forensic investigation that Eskom's letter was based on, it had not seen the underlying report and therefore was unable to comment further. Eskom also sought to recover funds from other international companies that it accused of failing to deliver value for money or flouting state procurement rules during former President Jacob Zuma's nine-year rule. Deloitte and McKinsey are among those who have agreed to settle (Burkhard, 2020).

As in the case of Steinhoff and Tongaat, detailed findings of these 'investigations' have not been made public, nor is it clear if external investigators were consulted (Open Secrets, 2020).

Summative comment on corporate failures in South Africa

Corporate failures such as Steinhoff caused the public to doubt the auditing profession. Steinhoff suffered a major setback in 2017, with accounting irregularities resulting in an investigation. Top executives had been misrepresenting financial data and Deloitte had failed to act on time. In 2018, the VBS Bank failure highlighted the role of the auditors, KPMG. KMPG may be held responsible for a possible R1.89 billion lawsuit following its audit of VBS. In 2018, Nkonki also collapsed. Issues of auditor independence, unethical behaviour and a lack of corporate governance resulted in its failure. From 2017 to 2018, KPGM made many media headlines. Their involvement with the Guptas and the VBS Bank failure had a serious effect on their reputation as well as that of the auditing profession in general. KPMG has subsequently strengthened procedures in corporate governance, agreeing to follow additional criteria outlined in King IV and to nominate an INED to support the existing members of the EXCO. In 2019, Tongaat announced past activities that were of serious concern to the board and the auditors of the firm. It was found that their financial results had been overstated by R3.5 billion to R4.5 billion. The investigation of this case is still in progress. Very recently, Eskom announced that its auditors, PwC, owed them R95 million. Eskom claimed that PwC charged them for work that Eskom had already done themselves. The investigation is still underway.

Critical link to objectives of the study

This chapter described some of the worst financial corporate failures the UK, USA, Australia, the Netherlands and South Africa. The literature also disclosed how the lack of corporate governance in both the public entities and the auditing firms contributed to these failures. It is clear that the lack of governance structures in auditing firms contributed in one way or another to the corporate failures and how these then had an effect on the reputation of the auditing firms. It was also seen that in some corporate failures, the auditing firms did not survive, ultimately resulting the collapse of the audit firm, such as Arthur Andersen and Nkonki.

This supports the argument for the development of guidelines on corporate governance practices and oversight structures for auditing firms in South Africa, and why this study is so important.

The recent string of corporate scandals and failures, both locally and internationally, has raised concerns regarding the effectiveness of corporate governance systems, the quality of work performed and independence of external auditors as a key assurance provider, as well as the role of regulators in overseeing and holding external auditors accountable (Putzier, 2019).

3.3 Conclusion

It would be fair to conclude that while auditors, accountants and other professionals are facing ethical dilemmas in their business careers, necessary action needs to be taken (Kavrar & Yilmaz, 2017). According to David Evaratt, head of the Wits School of Governance in South Africa, a major challenge in trying to maintain probity in the auditing industry is that the industry appeared to prosper irrespective of the controversies, since these large corporations were no longer merely auditors. They were project managers as well as providing business services and positioned themselves as indispensable, particularly for governments. The KPMG controversy came to light not because of government interference, but because South Africans were tired of corruption. Evaratt hoped outside powers, such as the USA authorities where these auditing firms are based, would bring them to heel (Hosken, 2017). He added that large corporations have entered countries for too long, believing they were rulers of the world and could get away with anything (Hosken, 2017).

External auditors play a vital role in ensuring corporate governance and upholding ethical standards such as fair or fact-based reporting, honesty, reliability, accountability and objectivity. External auditors and their reputation are therefore crucial (Abedian, 2017). Accounting ethics is of great importance to experts in accounting and to those who rely on their services. Many who work in the accounting sector know that people who use their services, especially decision makers who use financial statements, expect them to be highly qualified, accurate and objective. "Ethics is one of the factors binding a society together", according to Arens, Best, Shailer, Fielder, Elder and Beasley (2005). However, in today's intensely competitive markets, it is difficult for auditors and many other practitioners to provide customers with high-quality audits, instead of holding clients and worrying about revenues. Auditors are typically employed and paid by the financial report issuing entity but the main beneficiaries of the audit are consumers of the documents. As a result, it is unclear how impartial an auditor can be if they are paid for providing non-audit services to their clients. Situational factors such as the field of employment or the role held in an organisation may prejudice an auditor's ethical sensitivity (Kavrar & Yilmaz, 2017).

There is no question that a company with good corporate governance procedures is less likely to encounter accounting violations (Kavrar & Yilmaz, 2017). There is more to good ethics than simply doing the right thing. It is also best practice in any company (Verschoor, 2005). Many members of the accounting profession claim that the reputation of the profession has been irreparably damaged by corporate scandals such as those mentioned above. The negative publicity that accountants have brought upon themselves has undermined the reputation of the profession. The role of watchdog played by auditors includes educating the public about the financial state of a business, whether good or poor, and needs a demanding, even adversarial, attitude against a client (Zekany et al., 2004).

South Africa has encountered situations where suspicious auditing has undermined corporate governance. Considering the nature of the work of auditors and their critical role, the compensation offered should be fair to allow them to conduct thorough and detailed reviews of the operations of an organisation. Reducing remuneration discourages lengthy, in-depth assessments, leading to superficial exercises that rely on management reports and explanations without having to check them (Maranga, 2018).

It is vital to have a credible board of directors. To be successful, the board must have the right combination of individuals, including members who understand the processes of financial accounting and auditing. Moreover, longstanding auditors are susceptible to compromise, especially when it comes to objectivity. The oversight board should implement internal controls in an audit firm to ensure good corporate governance. This would foster honesty, openness and accountability in auditing firms. Corporate governance may be illustrated through the EXCO, the oversight board and auditing. Accountants and auditors must protect shareholders' interests, enforce policies to ensure accountability and transparency and perform regular risk assessments. As stipulated in the Code of Ethics for Professional Accountants, the principle of independence must be observed between auditors and users of their reports. This ensures that the roles of a company are isolated so that the auditors are not subjected to circumstances in which they may struggle to offer an accurate and objective opinion. This division of duties plays a crucial role in building trust among stakeholders. Auditors act as one of the key protectors of corporate governance in any organisation (Maranga, 2018).

The following chapter discusses the current legal and corporate governance structure and practice of auditing firms to identify possible concerns and solutions in terms of audit firm corporate governance. The chapter also provides an international overview with a specific focus on South African auditing firms.

Chapter 4: CURRENT CORPORATE GOVERNANCE STRUCTURES AND PRACTICES AT AUDITING FIRMS

4.1 Introduction

Chapter 2 discussed the importance of corporate governance, as well as the different corporate governance codes applicable in the UK, USA, Australia, the Netherlands and South Africa. It also discussed the corporate governance codes, legislation and/or principles applicable to auditing firms. It was found that the UK is the only country with a corporate governance code specifically for auditing firms. Chapter 3 discussed the corporate failures that took place in the UK, USA, Australia, the Netherlands and South Africa. The literature also provided evidence that most of the corporate failures took place as a result of a lack of corporate governance at both the public entities and the auditing firms. Chapter 4 discusses the current legal and governance structures of auditing firms, internationally and in South Africa to understand the reasons why it is difficult for South African auditing firms to simply apply the available corporate governance codes, such as King IV. The review also explores what reforms would be necessary to improve the corporate governance at auditing firms.

Auditing firms across the world are generally structured as a partnership or a private corporation (Bradley, 2020; Shapiro, 2019). In South Africa, auditing firms also typically fall within these two categories. According to the IRBA (2020), the top nine auditing firms in South Africa, all of which have 20 or more partners, are either a partnership or a personal liability company (Inc.).

The APA No 26 of 2005 regulates the auditing profession in South Africa and states who is regarded as the owner of an audit firm. According to the APA, only individuals who are registered auditors are shareholders of the company and every shareholder of the company is its director. This brings us to the board composition of an audit firm. Auditing firms are diverse and have different board structures. It is important to distinguish between the board structure and the governance structure of an auditing firm, as these terms are referred to in the empirical study and questionnaire.

‘Board structure’ refers to the directors who are responsible for the day-to-day operations of the audit firm. Based on the fact that all the shareholders are directors of the audit firm, as per the APA, it would be impossible for large auditing firms to have a board of directors composed of all the directors of the audit firm. For this reason, many auditing firms elect a management committee or EXCO which is responsible for the day-to-day management of the firm. This board consists of elected directors of the firm and is generally not responsible for the oversight of governance, but only the day-to-day management of the firm and audit quality.

With reference to ‘governance structure’, some auditing firms appoint an independent board/committee to provide oversight and governance over the EXCO and the audit firm. This is mostly applicable in larger auditing firms. The governance structure is known as the ‘oversight board’ (for the purposes of this study) or the ‘supervisory board’ (mostly in the Netherlands) (as referred to in Chapters 1 and 2). The names of the governance boards could differ from one audit firm to the next. It is within this oversight committee that some auditing firms appoint INEDs to ensure that there is an independent oversight board.

One of the latest challenges with regards to audit firm structures is the fact that most auditing firms not only provide auditing services but are multi-disciplinary entities and provide other services as well, such as consulting and advisory services (Duffield, 2020). In the UK, auditing firms are being forced by the FRC to split their audit and advisory services from one another to ensure independence. According to White and Miller (2020), the UK’s dominant accounting firms must separate their audit units from other operations by June 2024 as the FRC seeks to respond to the shortcomings that led to the collapse of several companies. The FRC is asking the Big Four auditing firms, namely, KPMG, Deloitte, PwC and EY, to agree to operational separation to ensure audit practices do not rely on persistent cross-subsidy from the rest of the firm. The guidelines seek to prevent accountants from being influenced by other parts of a firm’s business that could divert the focus away from audit quality. It is time that there is a genuine cultural change within the auditing firms and that we do away from the mindset that auditors are ‘advisors’, but rather senior executives.

From this it can be seen that the role of the directors, the tone at the top and ethical leadership is becoming increasingly important in the auditing profession. Once auditing firms are split, it will be easier to apply strict corporate governance rules or regulations within the firms. Until then, however, there is a pressing need for reform in the auditing profession.

It is a common perception that the public misunderstands the auditors. The cases of wrongdoing have irreparably harmed the public image of the profession; yet positive cases where audit recommendations avoid company failures are not publicised (Mirshekary et al., 2005). For this reason, corporate governance guidelines specifically for auditing firms could enhance the public's perception of auditing firms and improve the corporate governance at auditing firms. The public would then be able to see the change and reform in those firms.

The following sections discuss the current legal and governance structures of auditing firms, with a specific focus on South Africa. Thereafter, the concerns arising from the current structure are discussed while the last section presents recommendations, as gleaned from the literature.

4.2 Current legal structure of auditing firms

This section focuses on the legal structure of auditing firms, such as partnerships or private corporations, with a focus on both international and South African auditing firms. The information on South African auditing firms is found in their integrated reports or transparency reports.

4.2.1 Audit firm legal structures

Audit companies are typically owner-managed associations (Bradley, 2020; FRC, 2010). Shapiro (2019) states that the vast majority of auditing firms has partnership agreements and the partners have opted to cede powers in those relationships to an EXCO and/or a managing partner. Defining management roles for partners and executive boards provides greater efficiencies in the day-to-day management of an organisation (Shapiro, 2019). Bradley (2020) confirms that partnerships are the most common form of accounting and finance firms. Two or more individuals own shares in the company in this type of corporate structure, and share in the profits.

The audit business can also be a sole proprietorship or a public corporation (Bradley, 2020). Sole ownerships are managed by businessmen who can hire part-time or seasonal staff to assist with the workload. Private corporations are both sole proprietorships and partnerships. 'Public enterprise', on the other hand, is a term used to describe an accounting firm which issues stock shares in the open market (Bradley, 2020).

As stated above, auditing firms have ties with top executives of organisations and these organisations may need strategic advice in other fields such as human resources and information technology. This results in having multi-disciplinary entities. Several accounting firms have expanded their services by hiring senior-level subject-matter experts in other fields to provide consulting advice and project research for existing audit clients. This helps the company to increase its per-client sales and expand its customer relationship (McDonnel, 2020).

According to the IRBA (2020), only two of the top nine auditing firms in South Africa are partnerships. The other seven auditing firms are structured as personal liability companies (Inc.). This is also confirmed by the information disclosed in the transparency reports of the top nine auditing firms.

4.2.2 Partners or directors of auditing firms

There can be various groupings of partners and directors, depending on a company's size and structure. These titles would each come with their own rights and privileges, especially as applied to income distribution and voting rights (Shapiro, 2019).

The audit partner is a CPA with a professional accounting company and a full equity partner. When an employee is admitted to the partnership, they make a financial commitment to buy interest in the partnership. The partner gets a share of the profits, usually equal to their ownership percentage. The audit partner signs and endorses the audit report and the firm's financial statements and the companies it represents (McDonnel, 2020).

Should an audit firm decide to appoint a managing partner to take care of the day-to-day operations of the firm, the firm can elect to offer more rights and decision-making powers to the managing partner than others. This is especially true of founding partners who usually maintain effective control of the company by arrangement (Shapiro, 2019). For businesses that have granted the managing partner substantial power, the partnership arrangement will set out specific decisions that the managing partner has the authority to make in their own right, beyond the day-to-day business decisions. For example, the partnership agreement may state that the managing partner has the authority to bring in lateral partners or conduct minor fusions without the approval of the EXCO or the partners as a whole (Shapiro, 2019).

The promise of becoming a partner and the related financial benefits motivate many employees to work long hours and make personal sacrifices for the company. Obtaining a partner title brings additional respect because it means a degree of seniority and experience. Specialist accounting firms, however, usually require audit partners to be CPAs, which forbids a subject matter expert from becoming a non-CPA partner in a particular field (McDonnel, 2020). This statement is also supported by the International Organisation of Securities Commissions (IOSCO) (2009), which states that the EU required that the majority of the voting rights in an audit firm be held by those permitted to undertake statutory audits within the EU (i.e. qualified auditors). Furthermore, the audit firm's internal governance framework must contain provisions stating that a non-auditor could never gain control of the firm. Similarly, in the USA, the individual states, which are responsible for licensing public accountants, have historically regulated audit firm governance and have long required that a majority of audit firm owners be licensed accountants (IOSCO, 2009).

Similarly, with reference to South African auditing firms, Deloitte (2019) states that the title of partner is granted only to the business owners. A partner must be a qualified chartered accountant (CA (SA)), registered with the SAICA and the IRBA (Deloitte, 2019). This is in accordance with the APA, which specifies that only persons who are licensed accountants (with the IRBA) can be audit firm shareholders (APA, 2005). As stated by McDonnel (2020), this results in the limitation that someone who is not a registered auditor, but a subject matter expert, could not be director or partner at an audit firm. This is also coupled with the challenge of appointing INEDs to the board or EXCO of an audit firm. This challenge is discussed further in section 4.5.

The way partners vote on the major business decisions is often debated in a partnership agreement. The most common form of voting is the percentage ownership measure, where a partner's vote is weighted by percentage based on their ownership of the company. Many voting techniques include voting per unit (that is equal to one vote per partner), voting on capital account balances and voting on the previous year's income base. Depending on the size of their business and the relationship structure, companies will determine which strategy is right for them. Nevertheless, agreements do not need to connect a firm to only one vote. It is not unusual for an individual to have various methods of voting on specific matters. Some problems will need a simple majority as well, while others will need a supermajority (Shapiro, 2019).

Partners hold some prerogatives and privileges, usually including the appointment of the managing partner and members of the EXCO, as well as the approval privileges for large transactions and expenditures. Significant transactions may also include integration into a smaller business, new partner acquisitions, partner expulsions and addressing major financial problems, such as loans exceeding approved amounts and capital spending above a certain level. Partners are still entitled to approve a merger and related organic transactions (Shapiro, 2019).

From the above literature it is clear that audit firm legal structures are diverse and differ from one firm to the next. What is evident is the fact that all the directors are shareholders and all shareholders have to be registered auditors with the IRBA. Each audit firm decides who will manage the day-to-day operations of the firm. Generally, this is either done by appointing a managing partner, or appointing an EXCO, which would have a similar role to that of a board of directors in a public firm. The next section examines literature on the governance structures of auditing firms, with specific reference to the executive board and the oversight board.

Summative comment

Auditing firms are generally partnerships or personal liability (Inc.) companies. According to the IRBA (2020), the majority of the large auditing firms in South Africa are personal liability companies (Inc.). Some auditing firms appoint a managing partner to take care of the day-to-day operations of the firm. According to the APA (2005), all the shareholders of the audit firm have to be registered auditors with the IRBA. All shareholders are regarded as directors and all directors are shareholders. Auditing firms generally appoint an EXCO to manage the day-to-day operations. In South Africa this is mostly known as the EXCO or the management committee. Very little information is provided on committees or structures responsible for governance and oversight of auditing firms. Some auditing firms argue that they need not comply with the codes of corporate governance due to the company structure (Aberian, 2019). This, however, is not true as King IV, from an application perspective, is a framework that can be adopted across listed and unlisted companies, profit and non-profit organisations as well as public and private entities (IoDSA, 2016).

Critical link to the research objectives

The objective of the study is to provide guidelines on corporate governance practices and oversight structures for auditing firms in South Africa. From the above, it is evident that the majority of large auditing firms in South Africa are personal liability companies (Inc.) and would therefore be able to apply corporate governance principles that are specifically designed for auditing firms. As mentioned, there are difficulties in appointing INEDs to the EXCO of an audit firm and therefore, guidelines which take these challenges into account would be ideal for the auditing profession.

4.3 Current governance structures of auditing firms

In order for an audit firm to be well managed and provide efficient, high-quality customer service, it needs to be well governed. The individuals who have decision-making power, how they are selected and when they give up control are all relevant governance provisions that should be considered in a well-written partnership agreement (Shapiro, 2019). Below is an explanation on the EXCO and oversight board of auditing firms.

4.3.1 The Exco

As stated above in section 4.2.2, all shareholders of auditing firms are also its directors. Some large auditing firms in South Africa have up to 195 partners, who are ultimately the directors of the firm (IRBA, 2020). It would be impossible to have an effective board of directors or EXCO of 195 members. For this reason, some large auditing firms elect directors to become members of the EXCO, which is responsible for the day-to-day management of the firm. Shapiro (2019) supports this statement, stating that an EXCO of an audit firm is usually the company's controlling body and has the power to make or delegate all decisions.

Shapiro (2019) adds that governance decisions are crucial for the smooth day-to-day operation of the audit business. This is supported by KPMG (2019), which states that leadership plays a vital role in demonstrating dedication to quality, ethics and honesty. The tone at the top refers to an organisation's senior leadership attitudes and actions, and it influences the atmosphere and the behaviour desired by all of the organisation's employees. The embodiment of the right attitudes and actions desired through the company is an acceptable, cohesive tone at the top. Auditing firms are professional practitioners and have professional responsibilities that also include a duty to behave in a manner that takes proper account of the public interest (FRC, 2010)

As stated in the APA (2005), only auditors registered with the IRBA are allowed to be shareholders in auditing firms. This means that any individual who is not a registered auditor cannot be a director or shareholder of an audit firm. Therefore, an individual who is a subject matter expert, but not a registered auditor, cannot be a member of the EXCO. This regulation also makes it very difficult to appoint a director who is independent to the EXCO.

A reason often advanced for limiting ownership of auditing firms to licensed accountants is that practitioners have a public interest mandate as a result of the conditions under which the law grants their licenses in most jurisdictions. Public accounting, given its importance to the public, has long been considered a learned profession requiring an acceptable level of competence (e.g. through education, experience and certification). Limiting majority ownership and control to individuals who meet acceptable licensing credentials arguably promotes competence and a culture of professionalism and prevents non-practitioners from influencing, through management or control, the attestation practice without having the attendant competence, professional obligations and experience (IOSCO, 2009).

If a firm were owned by a majority of non-practitioners, the economic desire to generate a high return on investment could create pressures for a firm to place increased focus on cutting costs in areas such as training, development of firm methodologies and best practices and national office or other technical expertise. Each of these actions could provide short-term economic improvements, but may have long-term negative effects on audit quality. Therefore, many believe that restricting majority ownership of auditing firms to practitioners who operate with a public interest perspective and who have a significant and direct vested interest in the continuing viability of the firm helps mitigate the effect of such economic incentives. As a result, requiring a majority of ownership by licensed practitioners may decrease the likelihood that outside owners could influence an audit firm's attestation practice (IOSCO, 2009).

For the reasons mentioned above, there is a need for an independent governance structure, such as an oversight board, which can be appointed internally and which can provide independent governance and oversight to the EXCO of the audit firm. Very few auditing firms use independent governance structures such as an oversight board for overseeing their management (IOSCO, 2009).

Securities regulators and legislators have recognised the value of independent oversight of an entity's management (IOSCO, 2009). The next section discusses oversight boards.

4.3.2 The oversight board

The oversight of an audit firm's management by an independent board, which could consist of non-practitioners, holds many benefits for the audit firm and its stakeholders. Such structures (like an independent oversight board) could be designed to improve investor protection against auditors' conflicts of interest and to reinforce auditor independence. For example, oversight boards, to the extent that they have controlling voting rights, may help strengthen protection against conflicts of interest by maintaining the public interest perspective within the affairs of the firm. In addition, the oversight board could be charged with oversight of the firm's independence and with management of conflicts of interest. The influence of an oversight board, comprising individuals of independent judgment, could also be established to ensure that management implements firm-wide policies and procedures designed to create consistency and performance as well as high levels of audit service quality (IOSCO, 2009).

According to the 2019 transparency report issued by KPMG, the responsibilities of an oversight board could include independent oversight of strategy execution, protecting and enhancing the audit firm brand and overseeing the management of the firm.

Independence on the oversight board is considered of utmost importance (Zattoni & Cuomo, 2007). Shapiro (2019) also notes that the number of businesses that adopt two-tier board structure (an EXCO and an oversight board) is gradually growing. As stated in Chapter 2, auditing firms in the Netherlands apply the two-tier board structure and their oversight boards are entirely independent of the auditing firms. This appears to add to the independence and corporate governance of the auditing firms, based on the relatively small amount of organisational problems they have faced compared to other countries (SAAPTI, 2020).

In Chapter 6, a detailed content analysis of large and medium-sized auditing firms in South Africa examines the EXCO and the oversight board structures that these auditing firms have implemented. Unfortunately, there appears to be very little independence in South African auditing firms.

Summative comment

Auditing firms elect directors to be members of their EXCO. The EXCO is responsible for the day-to-day management of the audit firm. According to legislation all directors on the EXCO have to be registered auditors, which makes the appointment of INEDs on the EXCO very challenging. For this reason, an independent governance structure, such as an oversight board could be appointed internally (in some auditing firms) and independent members can be appointed to this oversight board. The oversight board is generally responsible for independently governing and overseeing the EXCO and audit firm. This board structure is called a two-tier board structure. Unfortunately, in South African auditing firms there is room for improvement with regards to the appointment of oversight boards. More detail on this is provided in Chapter 6.

Critical link to the research objectives

The research objective of the study is to provide guidance for best practice on corporate governance for South African Auditing firms. It is clear that the oversight boards of the auditing firms lack proper structure and independence and that in some auditing firms these boards do not even exist. This is also supported by the findings in Chapter 6. In developing guidelines for auditing firms, through the newly developed audit firm governance guidelines, auditing firms might find it easier to appoint an independent oversight board that will provide governance and oversight to the EXCO of the audit firm and ultimately improve the service provided to the public interest.

4.4 Concerns about current audit firm governance structures

As seen in Chapter 3, many corporate failures resulted in the public and other stakeholders questioning the audit profession. SAAPTI (2020) agrees and states that the past few years have been marked by global incidents of corruption and organisational failures that have placed the audit profession under a negative spotlight. Questions on the quality of an audit, the role of auditing firms and their obligation to the public interest have been raised (SAAPTI, 2020). South Africa is not exempt from these doubts. Historically, the World Economic Forum has ranked South Africa very high in terms of the quality of its auditing and reporting standards (Schwab, 2016). The 2016–2017 Global Competitiveness Index rated South Africa first out of the 138 countries (SAAPTI, 2020; Schwab, 2016). Yet in 2018, South Africa fell to 55th place, leading to the country's decline in overall global competitiveness by 20 places (47th to 67th) over the same time (SAAPTI, 2020). This occurred amid questions about the quality of the services carried out by KPMG at the South African Revenue Services and an agency affiliated with the Gupta family (Cotterill, 2018a; Putzier, 2019). According to Nkuhlu (2020), KPMG South Africa enabled state capture through its rogue unit report which gave credibility to then South African Revenue Services Commissioner, Tom Moyane's agenda. He further states that KPMG's risk management failed them and argues that compliance with King IV would have significantly reduced the chances of the KPMG disaster.

Some of the concerns highlighted in the literature are discussed below.

4.5 No corporate governance code for auditing firms

Chapter 2 provided evidence of the lack of corporate governance codes for auditing firms. The Audit Firm Governance Code in the UK is the only code in the world that provides guidance on corporate governance specifically for auditing firms.

Many, if not all, auditing firms in South Africa welcomed King IV when it was published in November 2016 (IoDSA, 2016). The firms released numerous informative documents, offering their clients advice on how to incorporate the new values. The IRBA and SAICA are listed as members of the King Committee participating in King IV's process of content creation. Through numerous publications, interviews and press releases, the audit profession praised and supported King IV as a step in the right direction for the King Committee, setting the right example and tone from the top to contribute to successful ethics governance. It was strongly believed that the application of King IV would lead to companies that are good corporate citizens and are perceived as such (Nkuhlu, 2020; SAAPTI, 2020). Yet most of the auditing firms themselves did not apply King IV. This is confirmed by Nkuhlu (2020), who states that only a few, if any, of the auditing firms apply King IV. This could be due to the fact that there is no sector supplement for auditing firms in King IV, together with the difficulty of applying some of the principles. Auditing firms find themselves in the intellectual centre of consulting on corporate governance, yet very few have a reputable and compliant independent governance structure. Currently, auditing firms' organisational systems are flawed. Many firms claim that they do not need to adhere to corporate governance codes because their business model is based on a partnership (Aberian, 2019). In order to comply with corporate governance, auditing firms should have an oversight board with a majority of non-executive members, properly balanced with respect to the combination of competences (Aberian, 2019).

Chapter 3 provided evidence on how the lack of corporate governance codes for auditing firms has contributed to the corporate failures in the world. Unethical behaviour can be directly linked to this shortcoming. Globally, integrity is seen as the audit profession's bedrock. In South Africa, however, it has become more important than ever to demonstrate this concept because of a string of failures that has cast a negative spotlight on the audit profession (SAAPTI, 2020). These negative developments led South Africa's Auditor General, Kimi Makwetu, to announce in 2018 that the reputation of the accounting profession in the country is in the gutter (Accountancy South Africa, 2019).

The sections below describe the challenges that auditing firms face with regards to corporate governance, and more specifically independence.

4.5.1 Lack of independence

Nkuhlu (2020) strongly believes that individuals in auditing firms play a key role. He states that:

> …there's already audit committees, a board, auditors and regulators. There should be increased capacity and effectiveness in all these layers of governance. Each of these layers must carry the responsibility of these corporate failures (Nkuhlu, 2020:n.p.).

All of these layers have failed society and they need to be reviewed in order for their effectiveness to be significantly enhanced; it also comes down to individuals, independence and ethical behaviour (Nkuhlu, 2020).

There are two key issues with respect to independence within an audit firm. First, there is the independence of the auditor. The lack of independence emerges when the relationship between a partner and an audit client preclude a company from serving as that entity's auditor or otherwise decrease the confidence in the independence of the company. Second, there is the independence of non-executive directors. This refers to the concern that a partnership between an audit firm's INED and its shareholders could be inconsistent with the characteristics of INEDs (FRC, 2016).

According to the FRC (2016), with respect to the UK Audit Firm Governance Code, auditing firms are establishing their own auditor independence policies in order to help ensure compliance with the UK's Ethical Standards and other national requirements. If a corporation establishes its own criteria for INEDs to facilitate compliance with the independence of auditors, that criteria should be reported in its transparency report (FRC, 2016).

As for non-executive independence of an audit firm and its owners, a range of relationships that may trigger a concern for independence would already be precluded in the provisions of auditor independence (FRC, 2016). However, as there are no clear requirements that define non-executive independence, the audit firm should reveal the criteria for determining whether its INEDs are independent of the company and its shareholders. These should include any time limits that apply to the company. If an INED has served longer than nine years, this should be subject to specific thorough scrutiny and should also be reported in the company's transparency report (FRC, 2016).

INEDs should not be prohibited from monitoring the processes of an organisation, for example, by serving on a remuneration committee, provided that they are unable to control any individual's compensation and/or recuse themselves from any situation where this may occur (FRC, 2016).

A firm is supposed to represent the views of an impartial, rational and knowledgeable third party when establishing criteria. Organisations should not therefore exclude individuals from consideration as possible INEDs solely on the grounds that issues of independence could arise in the future (FRC, 2016). Nonetheless, for these reasons, a current partner or staff member would never be deemed autonomous, so a plan to nominate a former partner or employee would need to be carefully considered (FRC, 2016).

Once named, INEDs would need to be alert to possible conflicts of interest, report back on them and ensure that they are exempt from all relevant decisions. An INED, for example, who also sits on a company's board contemplating hiring the audit firm as an auditor, may deny any participation on either side in the tender process. INEDs may also need to comply with applicable standards such as insider trading laws in relation to information they may become aware of through their association with a company (FRC, 2016).

According to the FRC (2010), the appointment of INEDs in auditing firms reflects the belief that regulation is not a replacement for effective governance but rather that good governance supplements regulation in the promotion of audit quality (FRC, 2010). Auditing firms also share operations, products and reputations with companies that are subject to little or no regulation and this may present major risks to the firm's credibility and continued life and its audit practice. This is where INEDs can play a part in helping to resolve such risks, as well as raising trust in the decision-making of companies and ensuring that stakeholder concerns are adequately addressed at the highest level (FRC, 2010).

4.5.2 Challenges in appointing an independent oversight board

A study by the IRBA found that 25% of the top 40 JSE companies had named members who had previously been employed by the external auditor as chairs of their audit committees, thus posing a challenge to the independence of the appointed auditor (Crotty, 2017). Two major concerns regarding independence in auditing firms were highlighted in Section 4.5.1, namely, auditor independence and the independence of INEDs. Due to the difficulty of finding directors who are fully independent of the audit firm and the audit clients, the UK Audit Firm Governance Code makes provision for auditing firms to determine the criteria of an INED according to the firms' purpose.

Summative comment

Chapter 3 demonstrated how the lack of corporate governance at auditing firms contributed to corporate failures and in some instances, to audit firm failures. This chapter explored the concerns that are most prominent with regard to audit firm governance. These include (1) the lack of a specific corporate governance code for auditing firms, (2) how to determine the independence of a director appointed to an audit firm board, and (3) the lack of independence on oversight boards that have been implemented at some auditing firms. It was also highlighted that even though most large auditing firms have oversight boards, there is still very little independence on these boards.

Critical link to the research objectives

The above concerns and challenges with regard to corporate governance at auditing firms are taken into consideration when developing guidelines on corporate governance practices and oversight structures for auditing firms in South Africa. The guidelines make specific reference to independence and independent oversight boards.

4.6 Suggestions for improving audit firm governance structures

The following sections provide suggestions on improving the audit firm governance structures. These suggestions include more independence through supervisory boards, the implementation of ISQM 1, considerations by SAAPTI and the release of a transparency report.

4.6.1 Independence through supervisory boards

A study undertaken by SAAPTI (2020) found that a number of significant initiatives has been adopted in the Netherlands. These have not been enforced in South Africa, which should be given consideration. Some of those recommendations include the appointment of an independent oversight board which is mainly concerned with the governance and oversight of the executive management and the audit firm (SAAPTI, 2020). Nkuhlu (2020) also feel very strongly that auditing firms should appoint INEDs to provide more effective oversight.

In Chapter 6 provides a detailed content analysis that examines whether South African auditing firms have appointed a South African oversight board. It can be said that not all auditing firms in the sample appointed oversight boards. In cases where there is such a board, there is very little independence.

4.6.2 Implementation and application of ISQM 1

As stated in Chapter 2, ISQC is the current standard for auditing firms, which discusses governance and leadership, but not the governance structures and practices. Since the release of the ISQC, the IAASB has produced a newly updated standard and released an Exposure Draft (ED) for ISQM1 which states that the current ISQC 1 does not explicitly address firm governance or contains much information on what is required of firm leadership in relation to firm governance. The updated standard, ISQM1, includes numerous suggestions to address firm governance and enhance the role of firm leadership in sustaining and continuously improving audiences. However, it is emphasised that any acts related to firm governance should be flexible in order to satisfy various jurisdictions and structures of companies.

The IAASB believes that governance and leadership of an organisation are of vital importance for quality service, as this is the way in which a company embeds its culture and ethics in how decisions of the business are made. Accordingly, the component of governance and leadership was first put in ED-ISQM 1. Governance of a firm often influences the view of the firm by the public, and a firm without successful governance may be viewed as not serving the public interest. In designing the various quality targets and responses, the IAASB indicates that it considered numerous global tools addressing governance and leadership for all organisations in general and those more relevant to auditing firms' governance. ED-ISQM 1 was greatly improved to strengthen the governance and leadership of auditing firms. It discusses in particular the desired actions of firm leadership in setting the tone at the top, the required leadership skills and keeping leadership accountable through performance assessments. The updated standards also discuss the effect of the company's strategic actions, including financial and operational decisions, on the level of service and the role of the company in the public interest, as well as the capacity of firm leadership to influence decisions about the company's resources (SAAPTI, 2020). As mentioned in Section 2.3, the ISQM is still in draft format and at the time of the study, was not yet enforced.

4.6.3 Considerations of the South African Auditing Profession Trust Initiative (SAAPTI)

SAAPTI's recommendations, which are still in draft format, include companies setting the following quality goals. These goals should address the company's environment, supporting the design, execution and operation of the other components of the quality management system, including the company's culture, decision-making processes, behaviour, organisational structure and leadership.

- The organisation's culture should be dedicated to quality, through appreciation and affirmation of professional ethics, principles and behaviours in the organisation. The responsibility of all staff for quality in the execution of quality management commitments or activities is stressed.
- The organisation should be responsible and have transparent leadership over quality.

- The strategic decisions and activities of the organisation, including financial and organisational goals, should reflect dedication to quality and the role of the organisation in serving the public interest through clear quality commitments.
- The organisation should have an organisational structure with the proper assignment of roles, responsibilities and authority, supporting the company's commitment to quality and the design, implementation and operation of the company's quality management system.
- The organisation should plan its resource requirements, including financial resources and obtain or allocate resources in a manner that maintains the company's dedication to quality and allows the design, implementation and operation of the company's quality management system.
- The organisation should fulfil its obligations in compliance with the relevant rules, legislation and professional practices relating to the company's governance and management.
- The organisation should design and execute solutions to resolve the quality risks found and evaluated by the organisation in relation to the goals of governance and quality of leadership.
- The organisation should develop, align and enhance ISQM1 transparent governance mechanisms for the audit sector with a strong duty to behave in the public interest (SAAPTI, 2020).

4.6.4 Release of transparency reports

The IRBA has been calling on South African auditing firms to voluntarily release transparency reports. The regulator must also collaborate with auditing firms and transparency report users to decide what the minimum contractual criteria should be for auditing firms to issue such reports annually. These reports allow consumers to understand a company's commitment to audit quality, leadership, culture and ethics, risk management procedures, employee and service provider relationships and independence. They also review the internal and external inspection and surveillance outcomes of the companies (IRBA, 2019).

While still to be approved in South Africa, businesses are required to voluntarily submit transparency reports for their operations (IRBA, 2018). However, despite these attempts to strengthen corporate governance in auditing firms, to date there is no corporate governance code in South Africa explicitly for auditing firms.

Summative comment

With the audit profession being in the spotlight after many corporate scandals, suggestions have been put forward on audit firm governance. These include (1) the voluntary release of transparency reports, (2) the development of the new ISQM 1 which places greater focus on the leadership and management of auditing firms, (3) suggestions by SAAPTI on improving governance at auditing firms, such as the establishment of an oversight board and (4) greater independence on the oversight boards of the auditing firms.

Critical link to the research objectives

The empirical study makes specific reference to an oversight board, its composition and responsibilities. Reference is also made to the release of a transparency report and the information it should include. From the findings of the empirical study, guidelines on corporate governance practices and oversight structures for auditing firms in South Africa are suggested.

4.7 Conclusion

Auditing firms are generally structured as partnerships or personal liability (Inc.) companies. Most auditing firms elect directors to be members of the EXCO who are responsible for the day-to-day operations of the firm but not its governance. Due to the requirements in the legislation, all shareholders and directors of auditing firms have to be auditors registered with the IRBA. This makes it difficult to appoint INEDs to the EXCO. For this reason, there is a need for the internal appointment of an independent oversight board, which would provide independent governance and oversight to the EXCO and the audit firm. Because there is no specific corporate governance code for auditing firms in South Africa, auditing firms have applied very little corporate governance principles and not all firms have appointed oversight boards. The Netherlands has seen the benefits of appointing supervisory boards that are 100% independent from the audit firm. The appointment of such boards is considered in the guidelines on corporate governance practices and oversight structures for auditing firms in South Africa.

In the IRBA's 2019/2020 Annual Report, former CEO Bernard Agulhas, claims that governments and audit authorities are now calling for changes internationally and are keenly examining recommendations and research on reform of the audit profession and how it is governed. He states that the IRBA is specifically focusing on developments in the UK. The current negative state of the profession brought on by the unprofessional actions of a few has undermined trust in the auditing profession. He said the regulator would work even harder to restore confidence and make the profession one of the most trusted and valued once again. The auditing industry was called on to review current practices to restore faith in the profession. Such trust is strengthened when all participants in the financial reporting chain, including management, those in charge of governance and investors, assume the obligation to rebuild the requisite trust (IRBA, 2019).

IRBA Chairman, Abel Dlamini, believes that everyone should work together and decide to make significant improvements to the profession to restore faith and trust (IRBA, 2019). The aim of corporate governance is to help create an atmosphere of trust, openness and accountability required to promote long-term investment, financial stability and business integrity, thereby promoting stronger growth and more inclusive societies (OECD, 2015a; Putzier, 2019). This is the ultimate objective of auditing firms and a good reason why guidelines on corporate governance practices and oversight structures for auditing firms in South Africa should be developed.

The following chapter discusses the research methodology applied in the study.

Chapter 5: RESEARCH METHODOLOGY

5.1 Introduction

In Chapter 1, it was stated that the objective of this study is to provide guidance to auditing firms on corporate governance practices and structures. The methodology consisted of a comprehensive literature review that identified and discussed the development of corporate governance in the UK, USA, Australia, the Netherlands and more specifically South Africa, the corporate failures in these countries and the current legal and governance structures of auditing firms. From the literature review, a comparative analysis was conducted of the UK Audit Firm Governance Code and King IV. This comparison provided the basis for the principles that are tested empirically in the content analysis and the questionnaire. The empirical study followed a two-phase approach: firstly, a content analysis was performed on the transparency reports and/or the integrated reports of the top nine auditing firms in South Africa. Secondly, an analysis was conducted on the questionnaires sent to the CEOs of the top nine auditing firms.

According to Kothari (2004), a research methodology is a way of systematically solving the research problem. It can be understood as the science of studying how research is conducted scientifically and includes various steps that are adopted in examining the research problem, along with the logic behind them. The methodology used in this study can be described in terms of the different steps in the research process. These steps include identifying the research problem, conducting the literature review, preparing the research design, selecting a sample, sample design, collecting the data and analysing and interpreting the data. This chapter provides a detailed explanation of the research methodology. The results of the empirical analysis are introduced and addressed in Chapter 6 while Chapter 7 presents the findings and suggestions that arise from them.

5.2 Theoretical framework

This study sought to establish corporate governance guidelines for large and medium-sized auditing firms in South African. The guidelines were centred on how auditing firms in South Africa could improve their corporate governance structures and act as custodians of corporate governance to look after the public interest. To achieve the research objectives, both the stakeholder theory and the shareholder theory were considered as the best suited to the purposes of the study. As discussed in Chapter 2, the stakeholder theory was found to be the most appropriate for the suggested corporate governance guidelines. This theory was incorporated into the design and development of the checklist and questionnaire of the study.

5.3 Research paradigms

The philosophic aspects of the social sciences are viewed through study paradigms. A paradigm is a collection of fundamental assumptions and beliefs as to how the world is viewed, which then directs the researcher's actions (Jonker & Pennink 2010). Study paradigms are considered as a collection of principles and practices that direct the researcher in the research process (Ackermann, 2014; Doyle, Brandy & Byrne, 2009; Harrits, 2011). Ackermann (2014) and Doyle et al. (2009) state that a specific paradigm is defined by three factors: (i) epistemology – how we perceive what we know, (ii) ontology – the nature of reality and (iii) axiology – the principles of the researcher. Moreover, there are three large paradigms of science that positions a researcher: (i) positivism – quantitative paradigm, (ii) constructivism – qualitative paradigm and (iii) pragmatism – mixed process paradigm (Ackermann, 2014; Doyle, Brandy & Byrne, 2009; Harrits, 2011). Below is a detailed explanation of each paradigm as well as the paradigm selected for this study.

5.3.1 Positivist paradigm

Positivism is often referred to as a scientific method or study of science based on the rationalist, empiricist theory of Aristotle, Francis Bacon and John Locke, to name a few (Mertens, 2005). It represents a determinist philosophy in which causes are likely to determine outcomes (Creswell, 2003). Positivists attempt to test a theory or describe an occurrence through observation and calculation to predict and monitor the forces that surround us (O'Leary, 2004). Positivism was replaced by post-positivism after World War II (Mertens, 2005). Positivist and post-positivist analysis is most explicitly concerned with approaches to quantitative data collection and interpretation (Mackenzie & Knipe, 2006).

Stahl (2007) defines the philosophy of positivism as a study theory centred on the ontological concept that reality is independent of the observer. Ontological assumptions form the most essential conceptual foundations of how the universe is interpreted (Stahl, 2007). For this reason, quantitative analysis is related to the positivist model (Aliyu, Bello, Kasim & Martin, 2014). Alessandrini (2012) specifies that, while qualitative data is favoured by the non-positivist or constructivist model, positivists prefer quantitative data. According to this model, facts can be created through observing numbers.

5.3.2 Constructivist paradigm

The constructivist model emerged from the philosophies of Edmund Husserl and his study of phenomenology, Wilhelm Dilthey's study of interpretive perception as well as the philosophies of other German philosophers known as hermeneutics (Eichelberger, 1989 as cited in Mertens, 2005). Constructivist methods of study seek to clarify the world of human experience (Cohen & Manion, 1994), given that reality is socially constructed (Mertens, 2005). The constructivist researcher focuses on the participants' impressions of the situation (Creswell, 2003) and acknowledges the importance of their own history and experience. In general, constructivists do not begin with a hypothesis during the research process (as with post-positivists), but rather produce or create a hypothesis or pattern of meanings inductively (Creswell, 2003). They do so in a manner that confirms or extends qualitative data and deepens the context (Mackenzie & Knipe, 2006)**.**

5.3.3 Pragmatist paradigm

As a study paradigm, pragmatism focuses on the notion that researchers should use a conceptual or methodological approach that is best-suited to the particular research problem under study (Tashakkori & Teddlie 1998). There is regular overlap between mixed methods or multiple methods research (Creswell & Clark 2011; Johnson & Onwuegbuzie 2004; Maxcy 2003; Morgan 2014; Teddlie & Tashakkori 2009), where the focus is not on the methods but on the consequences of study and research problems. Pragmatism can use both formal and informal rhetoric (Creswell & Clark 2011; Kaushik & Walsh, 2019).

Although it is not completely new to adopt pragmatism as a social science approach, the understanding of pragmatism has been enhanced by its widespread association with mixed methods research. In an investigative stage that underlies the search for knowledge, pragmatism points to the importance of joining values and actions (Kaushik & Walsh, 2019). Pragmatism treats science as a subjective experience based on the perceptions and actions of individual researchers (Morgan, 2014).

For the purposes of this study, a pragmatist paradigm is applied. More detail about the application of this paradigm (mixed methods) is discussed in the following section.

5.4 Research design and research methodology

5.4.1 Defining a research design

William and Donnelly (2006) defines a research design as the overall methodology used to coherently and logically integrate the different components of a study, thereby ensuring that the research issue is adequately addressed. This understanding is further supported by Kumar (2005), who observes that the research design is the model for data collection, estimation and analysis. De Vaus (2001) argues that the object of a research design is to ensure that the data allows the researcher to address the research problem as logically and unambiguously as possible. Bryman and Bell (2007) concur, stating that a research design offers a structure for the collection and analysis of data.

The research design selected for this study is explained below. The explanation considers the relevant paradigm, data collection method and data analysis technique.

5.4.1.1 Research design selected for this study

Mixed method analysis is typically a knowledge (theory and practice) approach that takes into account various viewpoints, positions and perspectives (Johnson, Onwuegbuzie & Turner, 2007).

A mixed approach, and more precisely, the simultaneous transformation triangulation model, is the research design selected for this study. Denzin (1978) first indicated how to triangulate methods, describing it as the combination of methodologies (always including qualitative and quantitative analysis perspectives) (Johnson, Onwuegbuzie & Turner, 2007). This design allows both quantitative and qualitative data to be collected simultaneously, which can then be combined to provide an overall picture of a phenomenon as part of the final discussion of findings (Ackermann, 2014; Edmonds & Kennedy, 2013; Grbich, 2013; Mamaile, 2018).

Morse (1991) demonstrated two types of methodological triangulation, namely, simultaneous triangulation and sequential triangulation. According to Morse (1991), simultaneous triangulation reflects the simultaneous use of qualitative and quantitative methods. There is little contact between the two data sources during the data collection stage; however, at the stage of data interpretation, the results complement one another. On the other hand, sequential triangulation is used when the findings of one approach are necessary for the preparation of the next approach (Johnson, Onwuegbuzie & Turner, 2007).

The data from all the sources is therefore complementary. An overview of the data transformation triangulation model adopted in this study is given in Figure 5.1 below.

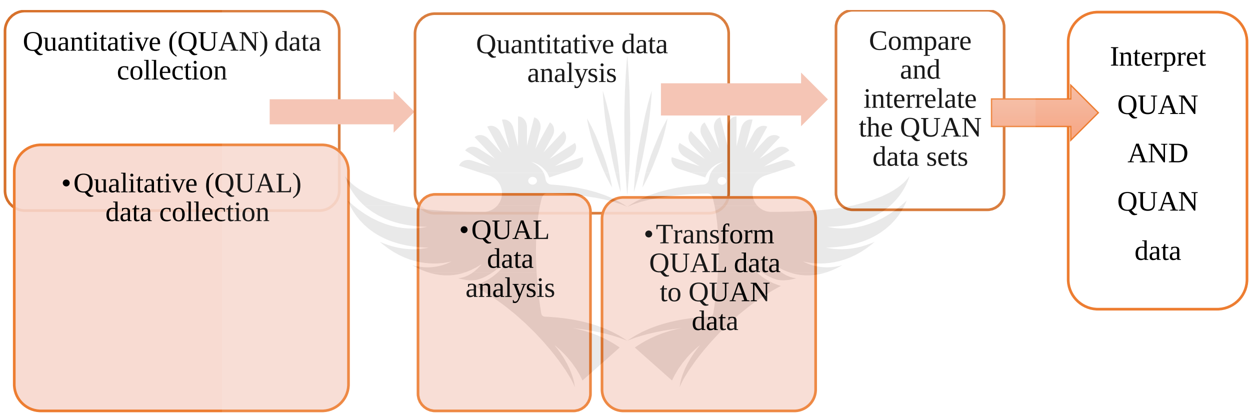

Figure 5.1: Data transformation triangulation design

Source: Ackermann (2014:146)

While recognising that triangulation may not be appropriate for all research purposes, Jick (1979) notes the following advantages of triangulation: (1) it allows researchers to be more confident of their findings; (2) it encourages the creation of innovative methods for collecting data; (3) it can lead to denser, richer data; (4) it can lead to the synthesis or incorporation of theories; (5) it can re-introduce theories; and (6) it can serve as a litmus test for contrasting viewpoints of ideas because of its comprehensiveness (Johnson, Onwuegbuzie & Turner, 2007).

During the analysis of this study, both qualitative and quantitative information was gathered. This data was independently analysed and the qualitative results were then converted into quantitative data that was correlated with the quantitative results.

5.5 Methods of data collection

The methodology used for data collection, which can be primary and/or secondary data, is outlined in this section. Leedy and Ormrod (2013) clarify that the process of data collection starts after defining the research problem and explaining the research design. Babbie and Mouton (2010) describe the processing of data as the assembly of quantitative numerical data or qualitative textual data (Flick, 2011). Therefore, data is empirical evidence or information carefully obtained in accordance with the study procedures (Neuman, 2011).

Pre-existing (or secondary) knowledge was gathered in this study. This form of data was originally collected for a different purpose and is reused for another research query (Hox & Boeije, 2005). Secondary data is thus publicly available. For the purposes of this study, the secondary data was collected through the literature review and content analysis.

Primary data refers to the information which was gathered directly from the participants, through the study questionnaires. The different methods used to collect the secondary and primary data are discussed below.

5.5.1 Secondary data collection

Secondary data is further defined as information collected by others for their specific purposes and made accessible to a wider audience, including researchers, through books, libraries and websites (Adams, Khan & Raeside, 2014; Diamantopoulos & Schlegelmilch, 2004; McCaston, 2005).

The secondary data for this study was obtained from publicly accessible data published on the websites of the auditing firms. It included the transparency reports and integrated reports. The secondary data was also collected by means of a literature review, conducted in Chapters 1 to 4. The content analysis which was performed is described in greater detail below.

5.5.1.1 Definition of a content analysis

Content analysis is a form of examining written, verbal or visual communication messages, according to Cole (1988) and Downe-Wamboldt (1992). This is supported by Cavanagh (1997), who notes that researchers consider content analysis as a flexible method for analysing text data.

Weber (1990) suggests that the study of material goes beyond merely counting words to extensive language analysis. The purpose of content analysis is to shed light in a phenomenon (Downe-Wamboldt, 1992). Harwood and Garry (2003) note that in the 19th century, content analysis was first used as a tool to analyse hymns, newspaper and magazine articles, advertisements and political speeches. Content analysis was later predominantly used as a quantitative research tool, with text data coded into simple categories and then statistically interpreted (Hsieh & Shannon, 2005). This technique is often referred to as qualitative data quantitative analysis (Morgan, 1993).

The seven steps typically followed in content analysis include (1) formulating the research questions, (2) selecting the sample, (3) specifying the categories to be used, (4) explaining the coding process and preparing the coder, (5) starting the coding process, (6) determining trustworthiness and (7) analysing the coding process. Content analysis depends significantly on the coding process. The basic coding approach in content analysis is to organise large amounts of text into much smaller categories of content (Weber, 1990). Categories are patterns or themes directly represented in the text or derived from it by research. Relationships between categories are the established. In the coding method, researchers using content analysis build or develop a coding scheme to direct coders to make decisions on content analysis (Kyngas & Vanhanen, 1999; Poole & Folger, 1981).

5.5.1.2 Application of content analysis in this study

For the purposes of this study, content analysis was selected as part of the collection of qualitative data. After conducting a comparison between the UK Corporate Governance Code and King IV (see Chapter 2, section 2.5 as well as Annexure I), a checklist was developed based on corporate governance elements that auditing firms are expected to disclose in their transparency reports and integrated reports. The checklist was then used to analyse the reports of the top medium and large auditing firms in South Africa. The check list also included information based on literature identified during the literature review.

As stated in the literature, at present, it is not compulsory for auditing firms to issue a transparency report in South Africa, however, the IRBA is in the process of making this compulsory for auditing firms. For this reason, not all the auditing firms had a transparency report. It should also be noted that the disclosure in the transparency reports do not reflect the actual governance practices at the auditing firms. The fact that auditing firms do not have to issue transparency reports, and that there is no guidance as to what information regarding governance should be disclosed by auditing firms, contributes to this point made by the researcher. More details about the analysis appear in Chapter 6.

The checklist can be viewed in Annexure M.

5.5.2 Primary data collection

The primary data for this study was collected by means of a questionnaire which was sent to the CEOs of the top nine auditing firms in South Africa. Below is a detailed explanation of the questionnaire data collection.

5.5.2.1 Questionnaire design and control

A self-completed questionnaire was used for the purposes on this study. In other words, the respondents answered the questions by completing the questionnaire online themselves. Both open- and closed-ended questions were included. For the open-ended questions, respondents could reply however they wished. For the closed ended questions, the answers were presented as a set of fixed alternatives from which they had to choose an appropriate answer.

The questionnaire was compiled using Google Drive and the Google Forms feature. The questionnaire was completed and presented to the participants (CEO's from the top nine auditing firms in South Africa) via a Uniform Resource Locator (URL) online. The questionnaire was then sent online and the respondents completed and submitted the questionnaire. The answers were then extracted from Excel and entered into the IBM Statistical Analysis Software Package (IBM SPSS) for analysis.

A mixture of polar questions, multiple choice questions and Likert scales was used in the questionnaire. Space was allocated under each section of the questionnaire in case the respondent wished to elaborate.

The SAAPTI provided a cover letter to show their support of the study. This letter, which was sent out with the questionnaire, can be found in Annexure L.

The questionnaire can be viewed in Annexure N.

5.5.2.2 Preparation, review and distribution

The questionnaire was compiled in July and August 2020 on the basis of a comprehensive literature review, in line with the problem and goals of study research. To ensure the validity, the questionnaire was sent for review to corporate governance experts, academics and audit practitioners in the field. After receiving excellent feedback from the pilot study, the questionnaire was finalised and completed on Google Forms. Once completed, a final test was performed by an independent academic in order to test the functionality of the questionnaire.

Communication with the auditing firms was made mid-September 2020 to invite potential participants to take part in the research. Emails were sent out containing the SAAPTI covering letter and the URL for completing the online survey using Google Documents. The survey was closed on 15 October 2020, after continuous follow-up by email and mobile.

5.6 Analysis of data

5.6.1 Qualitative data analysis

The latest transparency reports and integrated reports for the top nine auditing firms from 2018/2019 were obtained from their websites. In cases where such a report was unavailable on the website of the audit firm, the researcher sent the audit firm an email asking for a transparency report and an integrated report. These were the most recent reports available, as some of the 2020 reports were only published after this study was completed. These transparency reports and integrated reports were then read and analysed in depth and compared to the criteria on the checklist. Since there are only nine medium-sized and large auditing firms in South Africa, the researcher was able to conduct the content analysis by reading each report in depth.

5.6.2 Transforming qualitative data into quantitative data

Each of the transparency reports and integrated reports was analysed. The checklist contains a ‘yes’ and ‘no’ code asking whether the information stated in the checklist was present in the reports. This information was then used to quantify how many firms disclosed the relevant information as per the checklist.

5.6.3 Quantitative data analysis

To explain the meaning of the data together for all answers, descriptive statistics, frequency tables and graphs were used to explain the findings. Inferential statistics were not used because of the smaller sample. The findings were then correlated with the qualitative data that was transformed into quantitative data.

5.7 Validity and reliability of research

The results of the study contain both quantitative and qualitative data. Therefore, the validity, reliability (for quantitative data) and trustworthiness (for qualitative data) must be ensured.

Some scholars have proposed that qualitative studies should be measured or evaluated according to somewhat different standards to those used by quantitative researchers with regard to the reliability and validity of qualitative research. They suggest first assessing the trustworthiness of the analysis. Four criteria, each of which has an analogous criterion in quantitative analysis, make up trustworthiness. These include:

- Credibility, which parallels internal validity;
- Transferability, which parallels external validity;
- Dependability, which parallels reliability;
- Confirmability, which parallels objectivity (Bryman & Bell, 2007).

Establishing the credibility of results involves both ensuring that the study was carried out in accordance with good practice principles and submitting research findings to the participants in order for the participants to confirm that the researcher understood their feedback properly (Bryman & Bell, 2007). The findings from the analysis will be shared with all participants who confirmed they would like a copy of the results to maintain integrity.

Since qualitative research usually includes the extensive study of a small group or individuals who share certain features, qualitative results appear to be based on the contextual uniqueness and importance of the social environment being examined (Bryman & Bell, 2007). The fact that all auditing firms comply with the same regulations makes a major contribution to external validity. Even though the emphasis was on the top nine auditing firms with 20 or more partners, the findings are still transferable (see Section 5.8.3 on generalisation). In the work of Ackermann (2014), this rationale is also apparent.

Researchers should follow an ‘auditing’ method to determine the merit of research in terms of the criterion of trustworthiness. This includes ensuring that comprehensive records are held in an appropriate manner for all phases of the study (Bryman & Bell, 2007). All records were maintained for in this study. The study supervisor reviewed the report. Independent individuals were also used to verify that the content review results were a fair reflection of what was portrayed in the auditing firms’ disclosure reports and integrated reports.

Although full objectivity in business research is unlikely, confirmability seeks to ensure that the researcher acts in good faith. In other words, it should be clear that the researcher has not permitted personal beliefs or theoretical inclinations to manifestly affect the research results (Bryman & Bell, 2007). The researcher of this study remained impartial and neutral throughout the research process.

Internal validity, specifically material validity, was strengthened with regard to the quantitative findings through peer debriefing of the questionnaire by experienced academics and industry experts. Input from the reviewers was used to refine the questionnaires. Overall, it was determined that the questionnaire measured what it was meant to measure.

The data from the transparency reports and the integrated reports were used to corroborate and confirm the results of the questionnaire in order to enhance the validity of the findings. Therefore, overall, the study design contributed significantly to validity and trustworthiness.

5.8 Population and sample selection

The sampling frame for this study consisted of all the large and medium-sized auditing firms in South Africa. The sampling unit refers to each of the individual auditing firms in the sampling frame. The population for the study consisted of the medium and large sized auditing firms in South Africa, as determined by the IRBA (2020). These firms have 20 of more audit partners. The transparency reports and integrated reports of these auditing firms were obtained and the content analysis was performed. For the quantitative analysis, questionnaires were sent to the CEO's of each of these auditing firms. As the population of medium and large auditing firms was small, the whole population was used as the sample of the study.

5.8.1 Sampling design

In non-probability sampling, the sampling units do not have an equal opportunity to be included in the sample. The researcher thus purposely chooses sample units to be sampled from the sample frame. There are five distinct non-probability sampling methods, namely, quota sampling, accidental sampling, judgmental sampling or purposeful sampling, expert sampling, snowball sampling and modal instant sampling (Etikan & Bala, 2017).

'Expert non-probability sampling' was used for the study questionnaires. This refers to where the researcher receives the approval of others in the field of study who are experts or recognised experts and starts the process of gathering data directly from the person or group of respondents. The motives for the use of expert sampling are to provide a clearer way of constructing the opinions of people who are experts in a specific field (Etikan & Bala, 2017).

The sample consisted of the top nine auditing firms in South Africa, as confirmed by the IRBA (2020). These include:

- PricewaterhouseCoopers Inc.
- Deloitte and Touche
- KPMG Inc.
- Ernst and Young Inc.
- BDO South Africa Inc.
- Mazars
- SizweNtsalubaGobodo Grant Thornton Inc.
- A2A Kopano Inc.
- SAB and T Chartered Accountants trading as Nexia SAB & T (IRBA, 2020)

5.8.2 Sample size

The sample size of this study was 100% of the nine medium and large sized auditing firms, as per IRBA's classification (refer section 5.8.1).

5.8.3 Generalisability

Due to the fact that the whole population of auditing firms with 20 of more partners was used as the sample in the study, the findings cannot be generalised to other medium or large auditing firms in South Africa. Smaller auditing firms would have less partners, staff and clients. As a result, applying corporate governance guidelines may not be cost effective or affordable for smaller firms. A future study for smaller auditing firms could be considered. Another option is that should a corporate governance code be formulated based on the recommendations and guidelines of the study, the code could be based on a 'comply and explain' basis. In doing this, smaller auditing firms could apply the principles that they could and explain why other principles were not applied. The study can most definitely be generalised to other medium or large sized auditing firms in the world.

5.9 Ethics

Ethics can be described as the norms of behaviour that distinguish between good and reasonable behaviour and unacceptable behaviour (Östman & Turtiainen, 2016). Ethical considerations are important in research because by looking for the truth and fostering the ideal of trustworthiness ensures that researchers are responsible for their actions (Cacciattolo, 2015).

During this study, the researcher was honest when communicating with participants and in dealing with collected data. Every effort was made to remain unbiased during the data analysis phase and in all other areas where this was needed. Caution was taken during the research process to avoid errors and carelessness. The researcher was sincere in procedures used when obtaining data. Participants who asked to have access to the results were assured that a copy of the study would be sent to them. This was done in the interests of transparency.

The researcher was aware of intellectual property by giving credit where it was due and accepting any contributions produced by others. Informed consent was obtained from all the participants who had the right to stop their engagement at any time they wished to do so. The study data and information will not be used to damage any entity or any participant's credibility. At all times, the researcher aimed to prevent actions that would undermine the participants' confidence and treated all information as confidential. In addition, the companies' names were not revealed. Instead, numerical values were used as a means of identification, e.g. Organisation 1.

Prior to sending the questionnaire to the prospective participants, ethical approval was received from the University of Johannesburg. The certificate of ethical clearance can be viewed in Annexure J.

The security of the companies involved in this study was of the utmost importance. However, no ethical issues emerged as only publicly accessible sources of data were used and no modifications were made to the data.

5.10 Response rate

A 100% response rate was obtained for the content analysis for the firms that publish transparency reports and/or integrated reports. A 100% response rate was obtained for the questionnaire as all questionnaires were returned and completed in full.

5.11 Cut-off date

The cut-off date for the study was 31 August 2020. Any literature and developments made available after this date will be considered in future research.

5.12 Conclusion

This chapter provided an overview of the research methodology used in the study. A description was given of the research design and the triangulation design for data transformation. For both qualitative and quantitative data, the research methodology was clarified, mentioning the population, the sampling technique and measurement efficiency. The next chapter discusses the empirical results and findings.

Chapter 6: RESULTS OF THE EMPIRICAL STUDY

6.1 Introduction

This chapter presents the results of the qualitative and the quantitative empirical study. The results are examined with reference to the problem stated in Chapter 1. This is then used to provide a typical representation of the current status of corporate governance practices and disclosures in South African auditing firms as well as the expert opinions of the CEOs of the top nine auditing firms in South Africa regarding an Audit Firm Governance Code for South African auditing firms. The chapter first presents the qualitative findings obtained through a content analysis of the transparency reports and integrated reports of the top nine auditing firms in South Africa. The chapter then provides the quantitative results which were obtained through questionnaires sent to the CEOs of the top nine auditing firms in South Africa. Lastly the comparison (triangulation) between the qualitative and quantitative data is presented.

As stated in Chapter 5, Section 5.5.1.2, the checklist for the content analysis and the questionnaire were developed based on the UK Audit Firm Governance Code—currently the only audit firm governance code in the world. A comparison between King IV and the UK Code found that many of the King IV principles are already addressed in the UK Code, thus making it relatively easy for South African auditing firms to apply the principles. As King was initially developed based on the UK Cadbury report, it is submitted that the UK Audit Firm Governance Code could also be used as the foundation to develop guidelines for South African auditing firms. Hence, it was used to inform the checklist and questionnaire.

As stated in Chapter 1, the UK Audit Firm Governance Code contains six principles: (1) Leadership, (2) Values, (3) INED, (4) Operations, (5) Reporting, and (6) Dialogue (Financial Reporting Council, 2016). Annexure I also provides a detailed summary of the UK Audit Firm Governance Code as well as all the principles and provisions contained in the Code.

The empirical findings have been grouped according to the principles in the UK Audit Firm Governance Code. The findings are thus discussed according to the following headings (for the qualitative and quantitative findings and the triangulation):

i. Leadership
ii. Values
iii. INEDs
iv. Operations
v. Reporting
vi. Dialogue.

The tables used to present the findings are in the following format:

	Reference to the UK Audit Firm Governance Code	**Yes**	**%**	**No**	**%**	**Total**	**Total %**
Requirement according to principle/provision in the UK Audit Firm Governance Code as per checklist or questionnaire.	Number in Code						

The first column represents the principles/provisions as contained in the UK Audit Firm Governance Code that were analysed in the content analysis and questionnaire. A detailed example of the checklist can also be viewed in Annexure M. The second column is a cross-reference to the number of the principle/provision contained in the UK Audit Firm Governance Code. The next columns provide the responses 'yes' or 'no' as well as the percentage of the population represented by this response. The final two columns contain the total of auditing firms and a total percentage, indicating the percentage of the population on which the analysis was performed.

6.2 Content analysis

This section contains a qualitative discussion on the disclosure of corporate governance structures and practices of the top nine auditing firms in South Africa, as indicated in their transparency and/or integrated reports. Only seven of the auditing firms published transparency reports; thus, the sample used in the content analysis consists of these seven firms.

Only two of the auditing firms published integrated reports; however, the information contained in these reports was duplicated in the transparency reports. To minimise duplication in the findings, the findings were combined for both reports. Thus, if the audit firm disclosed information in either the transparency report or the integrated report, it was regarded as disclosure of governance information.

The following sections will be discussed in detail below: 6.2.1 Release of transparency and integrated reports, 6.2.2 Leadership, 6.2.3 Values, 6.2.4 INEDs, 6.2.5 Operations, 6.2.6 Reporting and 6.2.7 Dialogue.

6.2.1 Release of transparency and integrated reports

The first objective was to establish whether the auditing firms published transparency reports and/or integrated reports on an annual basis. According to the literature, the publication of such reports is not compulsory in South Africa, although it is recommended by the IRBA. According to the IRBA (2019), the release of transparency reports allows consumers to understand the audit firm's commitment to audit quality, leadership, culture and ethics, risk management procedures, employee and service provider relationships as well as independence. The IRBA has been calling on South African auditing firms to voluntarily release transparency reports in South Africa. According to the FRC (n.d.), the disclosure of information in the transparency reports will provide investors with a holistic view of the governance of the company. The call for greater transparency and disclosure by auditing firms has been further validated by high-profile audit firm failures (e.g. the demise of Arthur Andersen) and the lack of confidence in the financial markets in the post-global financial crisis era (Huddart, 2013). Patel (2013) argues that transparency creates a level of non-secrecy and openness of information in companies. It is an effective way of protecting the interest of stakeholders by promoting disclosure of non-financial information to hold governing bodies accountable for the decisions that directly or indirectly affect them (Frederick, 2000; Fung, 2014). The Brydon Report also provides recommendations for greater disclosure to promote trust in the corporate auditing profession (Brydon, 2019).

Table 6.1 Reports published

	Ref to UK Code	Yes	%	No	%	Total	Total %
Transparency report	A.1.2.	7	77.80	2	22.2	9	100
Integrated report	A.1.2.	2	22.20	7	77.8	9	100

As can be seen in Table 6.1, seven of the auditing firms published transparency reports while only two published an integrated report. The two firms that published integrated reports also released transparency reports.

It was pleasing to see that the majority of the auditing firms issued transparency reports on an annual basis. This could be an indication that they were aware of the call from the IRBA to issue such reports and that they were already preparing themselves should the IRBA make it compulsory for auditing firms to release these reports annually. However, it was concerning that one of the firms that failed to issue a transparency report is regarded as one of the bigger auditing firms in South Africa. The other firm that did not issue a transparency report is regarded as a smaller medium-sized audit firm. Both these firms did, however, indicate that they planned on issuing a transparency report in the near future.

The fact that only two of the nine auditing firms issued an integrated report could indicate that the firms were not yet ready to prepare such reports or alternatively, that they did not understand the purpose of these two reports. A suggestion could be made for auditing firms to combine these two reports to eliminate the duplication of information. One comprehensive report would add more value than two reports with duplicated information. This is also an indication that auditing firms need guidance, through a formalised corporate governance code, stating what information should be included in these reports. Such a code would also ensure consistency amongst the firms.

In the sections below (section 6.2.2 – 6.2.7) the findings of the content analysis are discussed according to the six principles of the UK Audit Firm Governance Code.

6.2.2 Leadership

Objective

According to the FRC (2016), the objective of the leadership principle is for auditing firms to display effective management, which has responsibility and clear authority for running the firm. Leadership also expects the management of a firm to be accountable to the firm's owners, with no individual holding unfettered powers of decision (FRC, 2016).

Findings

Table 6.2 Leadership disclosure in the transparency reports

	Ref to UK Code	Yes	%	No	%	Total	Total %
Available on the website	A.1.2.	4	57.14	3	42.86	7	100
EXCO information disclosed in transparency report	A.1.1.	7	100.00	0	0.00	7	100
Oversight board information disclosed in transparency report	A.1.1.	2	28.57	5	71.43	7	100

Source: SPSS output

Table 6.2 first indicates the platform used to publish the transparency reports. Four auditing firms published their transparency reports on their websites while three of the firms had to be emailed to request the transparency reports.

From the analysis of the transparency reports, it was found that seven of the auditing firms disclosed information about an EXCO but only two disclosed information about an oversight board.

Literature and deduction

As stated in the literature review, according to the IoDSA (2016), corporate governance is characterised by ethical and effective leadership. It requires those charged with governance to exemplify ethical leadership in discharging their responsibilities by demonstrating high levels of integrity, objectivity, competence, responsibility, accountability, fairness and transparency. At the same time, however, corporate governance requires those charged with governance to lead their companies towards the achievement of strategic objectives (IoDSA, 2016). Maseko (2015) adds that the boundaries of accepted behaviour for societies and organisations are set by effective leadership and corporate governance.

From the above discussion, it can be deduced that all auditing firms appointed an EXCO, and disclosed information about the EXCO in their transparency reports. The EXCO refers to the executive committee of the audit firm, and the members are selected from the partners of the firm. As stated in Chapter 4, a partner must be a qualified chartered accountant (CA(SA)), and registered with the SAICA and the IRBA (Deloitte, 2019). These appointment of INEDs to the EXCO can be challenging; very few auditing firms (only two) disclosed information about their oversight board. The oversight board is where the auditing firms appoint the INEDs, who ensure oversight and governance of the firm. Due to the difficulty of appointing INEDs in auditing firms, it is concluded that few auditing firms have appointed these independent boards. This could also be an indication that the auditing firms are waiting for reform in terms of the APA and additional guidance on how to appoint and implement more independent members in the firms.

Tables 6.3 and 6.4 illustrate the leadership provisions that are disclosed with reference to the EXCO and the oversight board.

Findings

Table 6.3 Leadership disclosure about the EXCO

Is the following be disclosed in the transparency report about the EXCO?	Ref to UK Code	Yes	%	No	%	Total	Total %
Duties	A.1.2.	2	28.57	5	71.43	7	100
Decisions made	A.1.2.	1	14.29	6	85.71	7	100
Job titles	A.1.3.	3	42.86	4	57.14	7	100
Election and appointment	A.1.3.	1	14.29	6	85.71	7	100
Terms	A.1.3.	1	14.29	6	85.71	7	100
Length of service	A.1.3.	2	28.57	5	71.43	7	100
Meeting attendance	A.1.3.	0	0	7	100.00	7	100
Biographical details	A.1.3.	0	0	7	100.00	7	100

Source: SPSS output

Table 6.3 illustrate the information disclosed by the auditing firms with reference to the EXCO. It indicates that two firms disclosed the duties of the EXCO members and one firm disclosed the decisions that were made by the EXCO members. Three auditing firms disclosed the job titles of their EXCO members. One firm disclosed information about the election and appointment of their EXCO members. One firm disclosed the terms of their EXCO members. Only two firms disclosed information about the length of service of their EXCO members. None of the firms disclosed information about meeting attendance or any biographical details of their EXCO members.

Table 6.4 Leadership disclosure about the oversight board

Is the following be disclosed in the transparency report about the oversight board?	Ref to UK Code	Yes	%	No	%	Total	Total %
Duties	A.1.2.	2	28.57	5	71.43	7	100
Decisions made	A.1.2.	2	28.57	5	71.43	7	100
Job titles	A.1.3.	3	42.86	4	57.14	7	100
Election and appointment	A.1.3.	1	14.29	6	85.71	7	100
Terms	A.1.3.	1	14.29	6	85.71	7	100
Length of service	A.1.3.	2	28.57	5	71.43	7	100
Meeting attendance	A.1.3.	1	14.29	6	85.71	7	100
Biographical details	A.1.3.	1	14.29	6	85.71	7	100

Source: SPSS output

Table 6.4 presents the information disclosed by the auditing firms about oversight boards. The table illustrates that two firms disclosed the duties of the oversight board members and two firms disclosed the decisions that were made by the oversight board members. Three firms disclosed the job titles of their oversight board members, one firm disclosed information about election and appointment of board members and one firm disclosed the terms of their board members. Two firms disclosed information about length of service while only one firm disclosed information about meeting attendance and the biographical details of its oversight board members.

Deduction

The above findings are proof that more structure and guidance should be provided to auditing firms with regards to leadership disclosure in the transparency reports. The firms disclosed very little information about their EXCO and oversight board and there were inconsistencies between the firms in terms of the information that was disclosed. This makes it difficult for the users of reports, as there is no standardisation of information that should be disclosed. Once again, it seems that auditing firms are willing to disclose information about their EXCO and oversight boards, but the lack of structure and guidance creates uncertainty as to exactly what should be included in the transparency reports.

6.2.3 Values

Objective

According to the FRC (2016), the objective of the value principle is that auditing firms should perform quality work by exercising judgment and upholding the values of integrity, objectivity, confidentiality and due care. They should exercise professional competence and behaviour in a way that properly takes the public interest into consideration and meets auditing and ethical standards. A firm should also maintain a culture of openness which encourages people to consult and share problems, knowledge and experience in order to produce quality work (FRC, 2016).

Findings

Table 6.5 Value disclosure in the transparency reports

	Ref to UK Code	Yes	%	No	%	Total	Total %
Code of conduct on website	B.1.3.	5	71.43	2	28.57	7	100
Discloses on the website to whom the code of conduct is applicable?	B.1.3.	5	71.43	2	28.57	7	100

Source: SPSS output

Table 6.5 shows that five auditing firms disclosed their code of conduct on their website, also indicating to whom the code of conduct was applicable.

Literature and deduction

As stated in the literature review, Sikka (2003) contends that audit failures are often the result of poor values prevalent in auditing firms. This view is supported by Peiter Koornhof of Allan Gray (an investment management company in South Africa), who states that major crises usually reflect a governance breakdown at multiple layers (Crotty, 2019). Sikka (2003) suggests that any reform of auditing and accountancy should bring about a major change in the values that govern auditing firms.

According to the IoDSA (2016), King IV is resolute in reinforcing the idea that corporate governance should be seen as a holistic set of principles that embrace ethical leadership, attitude, mindset and behaviour. The literature supports the notion that corporate governance guidelines for auditing firms would assist the firms in governing with the necessary values.

The empirical findings illustrate that auditing firms do disclose information about their codes of conduct and the values that govern the firms. However, the concerns stem from the application of these values. Due to the lack of a formal corporate governance code for auditing firms, these values differ from one firm to a next, thus creating inconsistencies. Once again, it is submitted that the values that govern the auditing firms should be formalised through specific guidelines or a corporate governance code for auditing firms.

6.2.4 Independent non-executive directors (INED)

Objective

According to the FRC (2016), a firm should appoint INEDs to its governance structure whose involvement would collectively enhance the firm's efforts to meet the principles of a corporate governance code. The INEDs' duty of care is to the firm (FRC, 2016). The following principles were analysed through the checklist in order to establish whether the INED principles were already being applied to some extent in South African auditing firms. The reader is reminded that the study focused on South African governance structures; thus, global oversight boards were not analysed.

Tables 6.6 to 6.9 indicate the information that the auditing firms disclosed about their INEDs. The principle of INEDs comprises separate provisions, including involvement of INEDs, disclosure of INEDs, characteristics of INEDs and the rights and responsibilities of INEDs. Tables 6.6 to 6.9 have been divided according to these provisions to ensure that the information is displayed in a logical manner.

Findings

Table 6.6 Involvement of INEDs: Content analysis

	Ref to UK Code	Yes	%	No	%	Total	Total %
Consists of majority of INEDs?	C.1.1.	0	0	7	100	7	100
Has at least three INEDs?	C.1.1.	2	28.57	5	71.43	7	100
Discloses reasons for not having at least three INEDs?	C.1.1.	0	0	7	100	7	100
Has a majority of INEDs who are members of other relevant governance structures in the firm?	C.1.1.	2	28.57	5	71.43	7	100

Source: SPSS output

Table 6.7 Disclosure about INEDs: Content analysis

	Ref to UK Code	Yes	%	No	%	Total	Total %
Appointment, retirement and resignation of INEDs	C.1.2.	1	14.29	6	85.7	7	100
Remuneration of INEDs	C.1.2.	1	14.29	6	85.71	7	100
Duties of INEDs	C.1.2.	1	14.29	6	85.71	7	100
INEDs' discharge of duties	C.1.2.	1	14.29	6	85.71	7	100
Firm support for INEDs	C.1.2.	1	14.29	6	85.7	7	100
How the firm positioned INEDs	C.1.2.	3	42.86	4	57.14	7	100

Source: SPSS output

Table 6.8 Characteristics of INEDs: Content analysis

	Ref to UK Code	Yes	%	No	%	Total	Total %
Has INEDs who have skills and experience in audit	C.2.	2	28.57	5	71.43	7	100
Has INEDs who are competent in auditing/accounting	C.2.1.	2	28.57	5	71.43	7	100
How INEDs impact on independence	C.2.1.	1	14.29	6	85.7	7	100

Source: SPSS output

Table 6.9 Rights and responsibilities of INEDs: Content analysis

	Ref to UK Code	Yes	%	No	%	Total	Total %
Discloses on its website procedures for dealing with any fundamental disagreement?	C.3.6.	0	0	7	100	7	100

***Source**: SPSS output*

Table 6.6 on the involvement of INEDs shows that none of the auditing firms had an oversight board that consisted of a majority of INEDs. Two of the auditing firms appointed at least three INEDs to their oversight boards. The five auditing firms that did not have at least three INEDs did not disclosed on their website why this was so. Only two of the auditing firms had a majority of INEDs who were members of other relevant governance structures in the firm.

Table 6.7 on the disclosure about INEDs shows that only one of the auditing firms disclosed the appointment, retirement, resignation, remuneration and duties of INEDs, how they discharged their duties and how the auditing firms supported the INEDs in this regard. The table illustrates that three of the auditing firms disclosed how the firms positioned the INEDs within the firm.

Table 6.8 on the characteristics of the INEDs reveals that two of the auditing firms had INEDs on their oversight boards with skills and experience in audit, and who were competent in the field of auditing and accounting. One only firm disclosed how its INEDs contributed to their independence.

Table 6.9 on the rights and responsibilities on INEDs indicated that none of the auditing firms disclosed procedures for dealing with any fundamental disagreement on their websites.

Literature and deduction

According to SAAPTI (2020), South African auditing firms should improve their governance structures through the appointment of an independent oversight board that is mainly concerned with the governance and oversight of the executive management and the audit firm. Nkuhlu (2020) strongly contends that auditing firms should appoint INEDs to provide more effective oversight.

A study by Uzun, Szewczyk and Varma (2004) examined how the occurrence of fraud was influenced by the company’s governance features and various characteristics of the EXCO. The study results indicated that the structure of committees and the composition of the EXCO had a significant effect on the occurrence of corporate fraud. The study found that the more INEDs on the board, the less likely the occurrence of corporate fraud.

According to the FRC (2010), the appointment of INEDs in auditing firms reflects the belief that regulation is not a replacement for effective governance but rather, that good governance supports regulation in the promotion of audit quality (FRC, 2010). At present, the corporate structures of auditing firms are flawed. Some auditing firms argue that they do not need to comply with the codes of corporate governance as their business model is based on 'partnership' (Aberian, 2019). According to Nkuhlu (2020), all auditing firms need to appoint INEDs and place risk and ethics under their oversight.

As stated in Chapter 2, the empirical study aims to provide guidelines on corporate governance practices and oversight structures for auditing firms in South Africa (based on the stakeholder theory and a two-tiered board structure), with principles that are specifically relevant to auditing firms. As the UK Code is currently the only audit firm-specific code in the world, the principles and provisions of this code were used in the checklist. This ensured that the checklist contained requirements that were relevant to auditing firms. Because of the APA, which only allows for registered auditors to be partners and shareholders of auditing firms, and members of the EXCO, it is not possible for auditing firms to appoint INEDs to their EXCO. Thus, there is a need for auditing firms to establish an independent oversight board. This results in auditing firms applying a two-tier board structure. By applying such a structure through the appointment of an oversight board, firms can still adhere to the APA and implement an independent governance structure.

It does seem from the above findings that very few auditing firms have implemented South African oversight boards. As stated earlier, only two firms have such boards, and of these, it seems that only one firm has implemented some of the INED principles and provisions, as stated in the UK Audit Firm Governance Code. The lack of independence and independent oversight of auditing firms is concerning. This is a definitive area that should be addressed by all medium and large auditing firms.

6.2.5 Operations

Objective

According to the FRC (2016), the objective of the operations principles is that a firm should comply with professional standards and applicable legal and regulatory requirements.

Findings

Table 6.10 Operations: Content analysis

	Ref to UK Code	Yes	%	No	%	Total	Total %
Policies and procedures to manage conflicts of interest exist?	D.1.3.	4	57.14	3	42.86	7	100
Effectiveness of the internal control system?	D.2.2.	2	28.57	5	71.43	7	100
Process followed in review performed?	D.2.2.	2	28.57	5	71.43	7	100
Weaknesses in internal control system?	D.2.2.	2	28.57	5	71.43	7	100
Actions to be taken to deal with weaknesses?	D.2.2.	2	28.57	5	71.43	7	100
How the firm will support its commitment to professionalism, openness and risk management?	D.3.	1	14.29	6	85.71	7	100
Whistleblowing policies and procedures?	D.4.	6	85.71	1	14.29	7	100

Source: SPSS output

Table 6.10 presents the information the auditing firms disclosed on their operations. Four of the firms disclosed information about policies and procedures to manage conflicts of interest. Only two firms disclosed information about the effectiveness of their internal control systems as well as the process followed to review the effectiveness of internal control systems. Only two firms disclosed the weaknesses identified within their internal control systems, and the actions taken to address these. One firm disclosed how it supported its commitment to professionalism, openness and risk management. Six of the firms disclosed information about their whistleblowing policies and procedures.

Literature and deduction

According to the IRBA (2019), transparency reports provide consumers with information on the company's commitment to audit quality, leadership, independence, culture, ethics, risk management procedures as well as employee and service provider relationships. The literature reviewed on the Netherlands also found that the corporate governance code in that country requires information on the quality of risk management systems. The literature thus confirms that the disclosure of operations in auditing firms is important. When referring to corporate failures at auditing firms, Nkuhlu (2020) states that KPMG's risk management failed the company. It can thus be argued that guidelines—issued through a corporate governance code for auditing firms in South Africa—could have mitigated corporate failures such as KPMG South Africa.

From the empirical findings on operations disclosure, is it evident that most of the principles discussed above are not disclosed by the majority of the auditing firms. This is concerning since auditing firms should disclose to the public and all stakeholders how their risks are managed and whether their internal controls are effective. As auditing firms serve a large part of the public interest, it is important to maintain transparency in their disclosure about risks and internal controls.

It should be noted that one audit firm had disclosed all of the above principles in its integrated report but not in its transparency report. This was therefore included in the findings as a 'Yes' with reference to the disclosure.

6.2.6 Reporting

Objective

According to the FRC (2016), the objective of the reporting principle contained in the UK Audit Firm Governance Code is for the management of a firm to ensure that members of its governance structures, including owners and INEDs, are supplied with information in a timely manner, and in a form and of a quality to allow them to discharge their duties. The principle also requires auditing firms to report on their compliance and non-compliance with the relevant governance code and publish, on an annual basis in its transparency report, a commentary on the firm's performance, position and prospects.

Findings

Table 6.11 Reporting: Content analysis

	Ref to UK Code	Yes	%	No	%	Total	Total %
Includes a commentary on the firm's performance, position and prospects	E.3.	3	42.86	4	57.14	7	100
Includes fair and balanced information	E.3.2.	4	57.14	3	42.86	7	100
Explains everything in an understandable manner	E.3.2.	6	85.71	1	14.29	7	100
Has an audit committee	E.4.1.	3	42.86	4	57.14	7	100
Has a risk committee	E.4.1.	5	71.43	2	28.57	7	100
Has a nomination committee	E.4.1.	2	28.57	5	71.43	7	100
Has a remuneration committee	E.4.1.	3	42.86	4	57.14	7	100
Has an ethics committee	E.4.1.	2	28.57	5	71.43	7	100
Audit committee constituted according to King IV	E.4.1.	1	14.29	6	85.71	7	100
Publishes audited financial statements	E.5.	0	0	7	100	7	100
Publishes audited financial statements prepared with the financial reporting framework	E.5.	0	0	7	100	7	100
Publishes audited financial statements that are clear and concise	E.5.	0	0	7	100	7	100
Explains who is responsible for preparing the financial statements	E.5.1.	0	0	7	100	7	100

Source: SPSS output

Table 6.11 presents the information that the auditing firms disclosed on their reporting. This refers to the way that the information was reported, the committees that the auditing firms reported on as well as the publication of audited financial statements.

Only three of the auditing firms included commentary on the firm's performance, position and prospects. Four firms included information that was fair and balanced. Six of the firms explained their information in an understandable manner.

With reference to committees, three of the auditing firms disclosed information about having an audit committee, five disclosed information about having a risk committee and two disclosed information about a nomination committee. Three of the firms disclosed information about a remuneration committee and two firms had ethics committees. Only one firm indicated that its audit committee was constituted according to the principles contained in King IV.

No evidence could be found of published audited financial statements nor was there any information regarding the reporting framework or who was responsible for preparing the financial statements. None of the firms disclosed that their financial statements were clear or concise. A further search was performed to determine whether the audited financial statements were possibly published on other platforms, however, no such evidence was found.

Literature and deduction

A study conducted by La Rosa, Caserio and Bernini (2018) found that investors are of the opinion that transparency reports provide meaningful information about audit firm quality and independence. According to the IRBA (2018), auditing firms are required to release transparency reports that provide information on certain elements of the firm and its operations.

The objectives of the UK Audit Firm Governance Code are to ensure that auditing firms are seen as examples of best practice governance, to encourage changes in the governance of auditing firms and to enrich auditing firms' transparency reports. Regulators and standard-setters maintain that transparency about the corporate governance of auditing firms will reduce information asymmetry between auditing firms and the public and will maintain a high quality audit service, thereby stabilising the capital market (Deumes, Schelleman, Bauwhede & Vanstraelen, 2012).

In 2018, the IRBA issued a call to auditing firms to release transparency reports disclosing the relevant internal information to the public. Such transparency reports are voluntary in South Africa (IRBA, 2018) and have been mandated only in a few countries. The majority of the research that is available was conducted in Europe where auditing firms have been subject to mandatory transparency reporting requirements since 2008 (Deumes et al., 2012; Pivac & Čular 2012).

The IAASB (2014) states that audit firm transparency reports assist third parties, such as the public and users of the audited financial statements, to understand the characteristics of individual auditing firms as well as the drivers of audit quality in those firms. They add that auditing firms can display to the public their approach to audits, thereby competing on aspects of audit quality (Deumes et al., 2012). The call for greater transparency and disclosure by auditing firms is further justified by high-profile audit firm failures (e.g. the demise of Arthur Andersen) and the lack of confidence in the financial markets in the post-global financial crisis era (Huddart, 2013).

To improve corporate governance, it is suggested that various committees be formulated within the organisations (Dedman, 2016). One-tier boards also often use board committees, such as audit, remuneration and nomination committees, to improve their corporate governance (Bendixen & Thomas, 2000; Maassen, 1999). Nkuhlu (2020) argues that individuals in auditing firms play an important role.

As stated above by the IoDSA (2016), transparency is an important element of corporate governance. According to the FRC (2019), it is critical that investors are able to assess the governance approach applied in an audit firm. Reporting on governance would cover the implementation of the principles of the relevant code with regard to the company's specific circumstances, how the board defined the mission and strategy of the company, reached targets and achieved results through its decisions (FRC, 2019). Corporate governance reporting should also relate coherently to other parts of the annual report so that shareholders can effectively assess the quality of the company's governance arrangements and the board's activities and contributions (FRC, 2019). In addition to providing stakeholder information, reporting promotes transparency and ensures that leadership reflects the primary governance and performance concerns it addresses (FRC, 2016).

The FRC believes that companies should review their transparency reports to provide information that is more applicable to investors, regulators and other stakeholders. In particular, companies applying the UK Audit Firm Governance Code should ensure that their report is fair, reasonable and comprehensible, and that it should include, among others, a description of how the EXCO and the INEDs worked throughout the year to fulfil the principles of the Code.

From the above empirical findings, only two of the provisions were implemented by the majority of the auditing firms. The findings on the understandability of the information in the reports could be subjective, and in this study, the assessment was based merely on the opinion of the researcher. Each user of the transparency reports of the auditing firms may have a different opinion. It was pleasing to see that five of the auditing firms disclosed information about having a risk committee. The other principles were not implemented by most of the auditing firms, which raises concerns. Once again, this could be due to the fact that there are no specific guidelines for auditing firms, explaining what information should be included in transparency reports as well as which committees should be established.

The fact that none of the auditing firms published its audited financial statements is also a concern. The public interest that these firms serve has no insights into the financial information of these firms. This too is something that could be addressed though formal guidelines for auditing firms.

6.2.7 Dialogue

Objective

According to the FRC (2016), the dialogue principle in the UK Audit Firm Governance Code seeks to ensure that auditing firms engage in dialogue with listed company shareholders as well as listed companies and their audit committees. The aim is to enhance mutual communication and understanding and make sure that the firm keeps in touch with shareholder opinion, issues and concerns.

Findings

Table 6.12 Dialogue: Content analysis

	Ref to UK Code	Yes	%	No	%	Total	Total %
Discloses policies and procedures for dialogue with listed company shareholders and listed companies?	F.1.1.	3	42.86	4	57.14	7	100
Discloses the nature and extent of the involvement of INEDs in the dialogue?	F.1.1.	1	14.29	6	85.71	7	100

Source: SPSS output

Table 6.12 presents the information that the auditing firms disclosed on dialogue. Three firms disclosed policies and procedures for dialogue with listed company shareholders and listed companies. Only one firm disclosed the nature and extent of the involvement of the INEDs' in the dialogue

Literature and deduction

The term 'governance' refers to the relationships between directors, shareholders, managers and sometimes employees (Aziri, 2014). The FRC (2019) maintains that a company's culture should be responsive to all stakeholders and shareholders, and should promote integrity and openness. Rossouw (2005) concurs, stating that the governing body is obliged to be accountable to stakeholders and shareholders.

From the above discussion, it can be seen that the auditing firms failed to disclose appropriate information with reference to the dialogue principle. The literature states that governance includes communication and involvement with shareholders and stakeholders. It is thus important that the auditing firms have regular dialogue with these parties and disclose the relevant information in their transparency report.

6.2.8 Conclusion

This section discussed the qualitative findings from the content analysis of the transparency reports and integrated reports of the top nine auditing firms in South Africa. Based on the findings, it can be concluded that the disclosure of the corporate governance information in the transparency reports and integrated reports was not always of the quality and quantity that would be expected of reputable companies.

The lack of disclosure reduces the reliance that stakeholders can place on the corporate governance of the auditing firms. This undermines public trust in the profession. The minimal disclosure by auditing firms confirms that auditing firms are not aware of the information they should be disclosing in their transparency reports. Consequently, there is a clear need for guidelines about the disclosure that is expected of auditing firms. Formal guidelines or a code would ensure that auditing firms disclose the right information in a consistent manner.

As can be gathered from the questionnaires administered to the CEOs of the top nine auditing firms in South Africa (discussed below in section 6.3), auditing firms appear to have done more with regards to corporate governance than the information they have disclosed in their transparency reports. This lack of quality and inconsistent disclosure can have negative repercussions for the auditing firms and the auditing profession as a whole.

In section 6.3, the quantitative findings are examined in greater detail. The triangulation model compares the qualitative and quantitative findings in section 6.4.

6.3 Questionnaires

The following section describes the results of the questionnaires that were completed by the CEOs of the top nine auditing firms. A 100% response rate was obtained for the survey.

The questionnaire consisted of two parts. The first part asked the participants about their current practice at their audit firm while the second part asked their expert opinion on a Corporate Governance Code for South African auditing firms (see Annexure N for the questionnaire). The findings from the questionnaire were also categorised according to the six principles contained in the UK Audit Firm Governance Code.

6.3.1 Leadership

Objective

The objective of these questions was to establish whether large and medium auditing firms in South Africa apply the provisions of the leadership principle, as contained in the UK Audit Firm Governance Code. An additional question was asked about the application of King IV. The CEOs were also asked to provide their expert opinions and commentary after each question.

Findings

Table 6.13 Leadership application in auditing firms

Application in the firm	Ref to UK Code	Yes	%	No	%	Total	Total %
EXCO	A.1.1.	9	100	0	0	9	100
Oversight board	A.1.1.	7	77.80	2	22.20	9	100
Issues a transparency report	A.1.2.	7	77.80	2	22.20	9	100
Issues an integrated report	A.1.2.	3	33.30	6	66.70	9	100
Governance disclosure in transparency report	A.1.2.	7	77.80	2	22.20	9	100
Performance evaluations	A.1.4.	6	66.70	3	33.30	9	100
Terms of reference (TOR) for the EXCO	A.2.	8	88.90	1	11.10	9	100
TOR for EXCO with authority over whole firm	A.2.1.	8	88.90	1	11.10	9	100
TOR disclosed on website	A.2.1.	2	22.20	7	77.80	9	100

Source: SPSS output

Table 6.13 presents the current practice of the leadership principle and provisions at the auditing firms. It can be seen that all the auditing firms indicated that they had an EXCO although only seven had an oversight board. Interestingly, seven of the firms indicated that they issued transparency reports, which is in line with the amount of transparency reports that were identified and analysed for the content analysis. Three auditing firms indicated that they issued integrated reports, which contradicts the only two integrated reports that were found for the content analysis.

Seven of the auditing firms indicated that they disclosed governance information in their transparency reports. Six stated that they provided information on performance evaluations of the members of the governance structure in their transparency report. Eight of the firms indicated that they had terms of reference for the EXCO, which included clear authority over the whole firm and its non-audit business. It is concerning that only two of the firms disclosed their terms of reference on their website.

Deduction

The findings of the content analysis and the questionnaire contradict each other. From the content analysis, it was found that two auditing firms had appointed oversight boards, yet in the questionnaires, seven of the auditing firms indicated that they had oversight boards. It could be that the auditing firms had appointed the oversight boards, but had not made the necessary disclosure in their transparency report. All the firms stated that they had implemented the necessary terms of reference, but only two disclosed this information on their website. Once again, there are inconsistencies between the firms with regards to disclosure, which could be eliminated through formal guidelines or a code.

The CEOs made the following comments on the terms of reference:

> "The terms of reference is [sic] part of our partnership agreement and Africa JV agreement."
>
> "Not sure if the terms of reference is [sic] on the website."
>
> "Largely due to the recent restructuring, we are in the process of establishing the frameworks etc."

The following question sought to establish whether the auditing firms applied some or none of the principles contained in King IV. Specifically, the question asked the extent to which the auditing firms had implemented corporate governance principles.

Table 6.14: Application of King IV principles in auditing firms

	Some	%	None	%	Total	Total %
Application of King IV	7	77.80	2	22.20	9	100

Source: CEO questionnaire (SPSS output)

Table 6.14 reveals that seven of the auditing firms' oversight board had applied some of the principles of King IV. Two of the firms did not have an oversight board, thus indicating that they did not apply any of the King IV principles.

From the additional comments received below, it is clear that one audit firm was applying more principles than some of the other firms. The CEO stressed that most of the principles had been applied. Three other auditing firms made the following comments:

"We do not have an independent board member and a Lead Director, however, all other principles are followed."

"Most of the principles, not only some."

"The independent members are not in the majority."

Table 6.15 provides the expert opinions of the CEOs on the leadership principle.

Expert opinions

Table 6.15 Disclosure in the transparency report about leadership

Should the following be disclosed in the transparency report?	**Ref to UK Code**	**Yes**	**%**	**No**	**%**	**Total**	**Total %**
Duties	A.1.2.	8	88.90	1	11.10	9	100
Decisions made	A.1.2.	8	88.90	1	11.10	9	100
Job titles	A.1.3.	9	100	0	0	9	100
Election and appointment	A.1.3.	9	100	0	0	9	100
Terms	A.1.3.	8	88.90	1	11.10	9	100
Length of service	A.1.3.	8	88.90	1	11.10	9	100
Meeting attendance	A.1.3.	8	88.90	1	11.10	9	100
Biographical details	A.1.3.	9	100	0		9	100

Source: SPSS output

Table 6.15 reflects the expert opinions of the CEOs of the top nine auditing firms and their opinion on the type of information which should be disclosed in the transparency reports about their oversight board. The feedback was very positive as eight of the CEOs indicated that auditing firms should disclose the duties, decisions, terms, length of service and meeting attendance for the members of the oversight board. All firms believed that the job titles and election and appointment methods of the members of the oversight board should be disclosed.

Deductions

The above findings indicate that auditing firms understand the importance of disclosing relevant governance information in their transparency reports. The majority (88.9%) of the CEOs indicated that leadership provisions should be disclosed in the auditing firms' transparency reports. Even though the firms did not disclose this information at present, the CEOs were of the opinion that the information should be disclosed. A formalised code or corporate governance guidelines would assist in the proper disclosure of such information by all auditing firms.

The CEOs of the auditing firms made the following comments:

"All of the above are critical information for transparency reasons."

"King IV, might not be entirely applicable to [the] audit firm environment and structure."

6.3.2 Values

Objective

The objective of these questions was to determine whether auditing firms apply the values principle and provisions contained in the UK Audit Firm Governance Code. The CEOs were also asked for their expert opinions on the provisions in the Code.

Findings

Table 6.16 Application of values in auditing firms

Application in the firm	Ref to UK Code	Yes	%	No	%	Total	Total %
KPIs for performance	B.1.2.	8	88.90	1	11.10	9	100
Code of conduct on website?	B.1.3.	6	66.70	3	33.30	9	100
Discloses on the website to whom the code of conduct is applicable?	B.1.3.	6	66.70	3	33.30	9	100

Source: SPSS output

Table 6.16 indicates the application of the value principle and provisions within the auditing firms. Eight of the auditing firms indicated that they had introduced KPIs for the performance of their governance system. Six firms indicated that they disclosed their code of conduct on their website and stated to whom the code applicable.

Expert opinions

Table 6.17 Responsibilities of the oversight board with reference to the value principle

Should the oversight board:	Ref to UK Code	Yes	%	No	%	Total	Total %
Upholds values of objectivity?	B.1.	9	100	0	0	9	100
Considers public interest?	B.1.	9	100	0	0	9	100
Complies with relevant standards?	B.1.	9	100	0	0	9	100
Promotes ethical culture?	B.1.1.	9	100	0	0	9	100
Assists with achieving an ethical culture?	B.1.1.	9	100	0	0	9	100
Oversees compliance with a code of conduct?	B.1.1.	9	100	0	0	9	100
Commits itself to a corporate governance code?	B.2.	9	100	0	0	9	100
Incorporates the principles of a corporate governance code into the internal code of conduct?	B.2.1.	9	100	0	0	9	100
Maintains a culture of openness?	B.3.	9	100	0	0	9	100
Provides oversight?	B.3.	9	100	0	0	9	100

Source: SPSS output

In Table 6.17, the findings represent the expert opinions of the CEOs on the application of the value principle. It is pleasing to see that all the auditing firms concurred that the oversight board should implement and practice all the principles mentioned above.

Deductions

The findings on the values principle were very positive. The application within the auditing firms was excellent, and the fact that the CEOs all agreed on the responsibilities that the oversight board should have with regards to values indicate that the firms understood the importance of these provisions. It is also an indication that the auditing firms were willing to implement such provisions should a corporate governance code for auditing firms be developed in future.

The CEOs of the auditing firms made the following comments:

“The oversight board should play a monitoring role, and should only take the lead when EXCO is not fulfilling its mandate in respect of the established Terms of Reference. A variety of committees such as Social and Ethics, Compliance and Governance, cover some of the matters raised above. Our experience is that additional layers of governance which may duplicate responsibilities will squeeze profitability even further, resulting in the auditing profession continuing to be an unattractive option for new entrants.”

“The above answers are provided on the basis that an oversight is mandatory for auditing firms—I am however of the opinion that the leadership of auditing firms are able to implement the required governance structures.”

“The oversight board can be valuable also in helping with restoring trust in the entire profession.”

“The oversight structure for an audit practice will have its nuances given that the shareholders are the partners in the firm (no external Investors). Serving public interest is the key priority. We support the Audit Quality Board as recommended by SAAPTI.”

“Auditing firms serve public interest and must therefore be governed the same as other PIEs.”

“Code of conduct monitoring is executive management’s responsibility; oversight board needs to make sure that executives do that.”

6.3.3 Independent non-executive directors

Objective

The objective of these questions was to determine firstly the application of the ‘independent non-executive’ principle as contained in the UK Audit Firm Governance Code. Secondly, it was also important to obtain the expert opinions of the CEOs on the INED provisions. These opinions are presented in the tables below.

Findings

Table 6.18 Application of INED principle in auditing firms

Application in the firm	Ref to UK Code	Yes	%	No	%	Total	Total %
Independent members on the oversight board?	C.1.	2	22.20	7	77.80	9	100
Indemnity insurance?	C.3.4.	6	66.70	3	33.30	9	100
Disclose on its website procedures for dealing with any fundamental disagreement?	C.3.6.	1	11.10	8	88.90	9	100

Source: SPSS output

Table 6.18 provides the findings on the appointment of INEDs to the oversight board of auditing firms. It was found that two of the auditing firms had appointed INEDs while six indicated that they had indemnity insurance in place in case of legal action against any INEDs. It seems that more auditing firms have implemented this precaution even though they may not yet have appointed the INEDs. It is concerning to see that only one audit firm disclosed on its website the procedures that should be taken for dealing with any fundamental disagreements between the INEDs and the firm’s management team or governance structures.

Expert opinions

The principle of INED is divided into four different sections, namely, (i) involvement of INEDs, (ii) disclosure of INEDs, (iii) characteristics of INEDs and (iv) rights and responsibilities of INEDs. As there are many provisions within this principle, the findings are presented according to these four sections as depicted in Tables 6.19 to 6.22.

Table 6.19 Involvement of INEDs: Expert opinion of CEOs

With reference to the INEDs on the oversight board	Ref to UK Code	Yes	%	No	%	Total	Total %
Consists of majority of INEDs?	C.1.1.	1	11.10	8	88.90	9	100
Has at least three INEDs?	C.1.1.	3	33.30	6	66.70	9	100
Has INEDs who oversee public interest matters?	C.1.1.	8	88.90	1	11.10	9	100
Has a majority of INEDs who are members of other relevant governance structures in the firm?	C.1.1.	3	33.30	6	66.70	9	100
Has INEDs who report on risk and audit quality?	C.1.1.	8	88.90	1	11.10	9	100

Source: SPSS output

Table 6.19 represents the findings on the involvement of INEDs in the audit firm. Interestingly, only one CEO believed that the oversight board should consist of a majority of INEDs while three CEOs stated that the oversight board should consist of at least three INEDs. Eight CEOs indicated that the oversight board should have INEDs who oversaw public interest matters. Three CEOs believed that the oversight board should have a majority of INEDs who were also members of other relevant governance structures in the firm. Eight CEOs indicated that the oversight board should have INEDs who reported on risk and audit quality.

Table 6.20 Disclosure about INEDs: Expert opinion of CEOs

With reference to the INEDs on the oversight board	Ref to UK Code	Yes	%	No	%	Total	Total %
Appointment, retirement and resignation of INEDs	C.1.2.	8	88.90	1	11.10	9	100
Remuneration of INEDs	C.1.2.	7	77.80	2	22.20	9	100
Duties of INEDs	C.1.2.	8	88.90	1	11.10	9	100
INEDs discharge of duties	C.1.2.	8	88.90	1	11.10	9	100
Firm support to INEDs	C.1.2.	9	100	0	0	9	100
How the firm positioned INEDs	C.1.2.	8	88.90	1	11.10	9	100

Source: SPSS output

Table 6.20 presents the information that should be disclosed about the INEDs on the oversight board. Eight CEOs believed that the appointment, retirement and resignation of the INEDs should be disclosed, seven believed that the remuneration of the INEDs should be disclosed and eight believed that the duties and how INEDs discharged their duties should be disclosed. All the CEOs concurred that auditing firms should disclose how they supported INEDs in discharging their duties. Eight CEOs believed that firms should disclose how they positioned INEDs, either on the EXCO or on the oversight board.

Table 6.21 Characteristics of INEDs: Expert opinion of CEOs

With reference to the INEDs on the oversight board	Ref to UK Code	Yes	%	No	%	Total	Total %
Has INEDs who command respect from owners	C.2.	8	88.90	1	11.10	9	100
Has INEDs who enhance shareholder confidence	C.2.	8	88.90	1	11.10	9	100
Has INEDs who have skills and experience in audit	C.2.	8	88.90	1	11.10	9	100
Has INEDs who are competent in auditing/accounting	C.2.	8	88.90	1	11.10	9	100
INEDs' impact on independence	C.2.1.	9	100	0	0	9	100

Source: SPSS output

Table 6.21 presents the opinion of CEOs about the characteristics that INEDs on the oversight board should possess. Eight of the CEOs strongly believed that the INEDs should command respect from the owners of the auditing firms, enhance shareholder confidence, have experience and skills in audit and should be competent in auditing and/or accounting. All the CEOs agreed that the audit firm should have criteria for assessing the impact of the INEDs on the firms' independence as auditors and their independence from the firm and its owners.

Table 6.22 Rights and responsibilities of INEDs: Expert opinion of CEOs

With reference to the INEDs on the oversight board	Ref to UK Code	Yes	%	No	%	Total	Total %
INEDs: Have rights	C.3.	9	100	0	0	9	100
INEDs: Have right to access information	C.3.	9	100	0	0	9	100
INEDs: Have right to access people	C.3.	9	100	0	0	9	100
INEDs: Have contract with their rights and duties	C.3.1.	9	100	0	0	9	100
INEDs: Be appointed for specific time	C.3.2.	9	100	0	0	9	100
INEDs: Review of independence	C.3.2.	9	100	0	0	9	100
INEDs: Oversee policies and procedures	C.3.3.	9	100	0	0	9	100
INEDs: Maintain firm reputation	C.3.3.	9	100	0	0	9	100
INEDs: Reduce risk of audit failure	C.3.3.	8	88.90	1	11.10	9	100
INEDs: Provided with authority	C.3.4.	9	100	0	0	9	100
INEDs: Provided with resources	C.3.4.	9	100	0	0	9	100

Source: SPSS output

Table 6.22 presents the opinions of the CEOs on the rights and responsibilities that INEDs on oversight boards should have. It is pleasing to see that all the CEOs agreed about the rights and responsibilities of INEDs. Only one CEO disagreed with the provision that INEDs should be tasked with reducing the risk of audit firm failure.

Deductions

From the above discussion, it is clear that the majority of the CEOs agreed about the importance of the provisions in the INED principle. The main disagreement regarded the 'involvement of the INEDs' provision. It can be seen that the majority of the CEOs did not believe that the oversight board should consist of a majority of INEDs, only three CEOs believed that the oversight board should consist of at least three INEDs and that the majority of the oversight board should consist of INEDs. The negative response to these provisions could be due to the fact that it is very difficult for auditing firms to identify and appoint individuals who are fully independent, as discussed in Chapter 4.

The CEOs of the auditing firms made the following comments:

Characteristics of INEDs:

"In a partnership set-up, it is still important to have [a] majority [of] independent executive members due to the nature of the practice."

"Auditing firms do not have external investors; the objective must be to create oversight structures that ensure the firm is focused on serving Public Interest, High Quality Audits, Strong Ethics and Culture."

"We should not be dogmatic about absolute number of non-executive directors."

Rights and responsibilities of INEDs:

"Should an independent non-exec have to rely on laws and regulations to access information and people, then the firm should consider whether they are ready for this type of governance. It should be available freely and willingly."

"Non-executive members of the oversight board can be helpful in restoring the trust in the profession."

"Independent non-executive directors should have same rights and duties as those of PIEs."

"We currently do not have a legal framework for oversight board."

6.3.4 Operations

The operations principle is explained in three separate tables because the responses in the questionnaire were different for some questions. The first two tables illustrate the current practice in the audit firm while the last table illustrates the expert opinions of the CEOs regarding the operations principle.

Objective

The objective of these questions was to determine whether the EXCO of the auditing firms applied and practised the operations principle and provisions as contained in the UK Audit Firm Governance Code. The questionnaire also sought the expert opinion of the CEOs of the auditing firms on the provisions in the Code.

Findings

Table 6.23 EXCO operations in auditing firms

Application in the firm by EXCO	Ref to UK Code	To a large extent	To a lesser extent	Totally ineffective	Total	Total %
Maintaining a sound system of internal control	D.2.	8	1	0	9	100
Maintaining a sound system of risk management	D.2.	8	1	0	9	100
Annual review of the system of internal control?	D.2.1.	5	3	1	9	100
INEDs reviewing all material controls	D.2.1.	3	1	5	9	100
INEDs promoting an appropriate culture	D.2.1.	2	2	5	9	100

Disclosure: Effectiveness of the internal control system	D.2.2.	4	2	3	9	100
Disclosure: Weaknesses in internal control system?	D.2.2.	2	4	3	9	100
Disclosure: Actions to be taken to deal with weaknesses	D.2.2.	2	4	3	9	100
Assessment of the principal risks	D.2.3.	7	2	0	9	100
Policies and procedures for managing people	D.3.	9	0	0	9	100
Disclosure: How does the firm support its commitment to professionalism, openness and risk management?	D.3.	6	2	1	9	100
Establishing whistleblowing policies and procedures?	D.4.	8	1	0	9	100
Disclosure: Whistleblowing policies and procedures	D.4.	6	2	1	9	100
Reporting whistleblowing issues to INEDs	D.4.1.	2	1	6	9	100

Source: SPSS output

Table 6.23 indicates that eight of the auditing firms maintained a sound system of internal control and risk management over the operations of the firm. Only five of the firms conducted an annual review of the effectiveness of the system of internal control, to a large extent and three firms to a lesser extent. One firm stated that it was totally ineffective, thus no annual review was conducted.

With reference to independence, only three auditing firms had INEDs who reviewed the material controls in the audit firm. One firm stated that this was done to a lesser extent, and the remaining five firms stated that this function was totally ineffective. Only two firms indicated that their INEDs promoted an appropriate culture which was underpinned by sound values and behaviour. Two firms indicated that this was done to a lesser extent, and five auditing firms indicated that this control was totally ineffective within their firms.

Four auditing firms indicated that they disclosed in their transparency report that a review was performed on the effectiveness of the internal control system. Two firms disclosed this to a lesser extent, and three auditing firms not at all. Four auditing firms indicated that they disclosed in their transparency report which process was applied to perform a review of the effectiveness of the internal control system. Two firms disclosed this to a lesser extent, and three firms not at all.

Two auditing firms indicated that they disclosed in their transparency report the weaknesses that were identified in the review of the effectiveness of the internal control system. Four firms indicated that they disclosed this to a lesser extent, and three firms did not disclose this at all.

Two firms indicated that they disclosed in their transparency report the actions that were taken to deal with weaknesses identified in the review of the internal control system. Four firms indicated that they disclosed this to a lesser extent but three firms did not disclose it at all.

Seven auditing firms indicated that they carried out a robust assessment of the principal risks the audit firm was faced with, described the risks and explained how they were being managed. Two firms indicated that they did this to a lesser extent. All the firms also indicated that they applied policies and procedures for managing people across the whole firm.

Six of the auditing firms indicated that they disclosed on their website how the firm supported its commitment to professionalism, openness and risk management. Two firms disclosed this to a lesser extent but one firm did not disclose this at all.

Eight auditing firms indicated that they established whistleblowing policies and procedures, but only six disclosed the policies and procedures on their website to a large extent. Two firms disclosed this to a lesser extent and one firm did not disclose any whistleblowing policies and procedures. Two firms indicated that they reported to the INEDs on issues raised under the whistleblowing policies and procedures. One audit firm did this to a lesser extent but six did not do this at all—most probably because of a lack of INEDs in the firm.

The CEOs of the auditing firms provided the following commentary on the above questions. Most of the comments addressed the presence of INEDs within the firm, once again highlighting the lack of independence in auditing firms.

> “The questions suggest that non-execs should be appointed to appropriate Boards. We have had this previously but IRBA were not in support of it.”
>
> “Our firm does not have any independent non-executive directors.”

"The process of appointing non-executive directors is underway and to be completed by end of June 2021."

"Many of the procedures mentioned above are dependent on the integration of our national firm, which is still in the early stages of development. We also do not have any independent directors on the governance council yet."

"The firm does not currently have non-executive directors. It does, however, have an independent chair of risk committee. The firm does not publish transparency report, it plans to do that from next year 2021. The global transparency report is, however, published on network."

"We do not have non exec directors."

Table 6.24 Application of operations principle in auditing firms

Application in the firm	Ref to UK Code	Yes	%	No	%	Total	Total %
Complies with professional standards and legal/regulatory requirements?	D.1.	9	100	0	0	9	100
Operations promote audit quality	D.1.	9	100	0	0	9	100
Policies and procedures for compliance	D.1.1.	9	100	0	0	9	100
Policies and procedures for signing audit reports to comply with applicable standards	D.1.2.	9	100	0	0	9	100
Policies and procedures for the reliance of other auditors' work	D.1.2.	9	100	0	0	9	100
Policies and procedures to manage conflicts of interest	D.1.3.	7	77.80	2	22.20	9	100
Takes action on concerns identified by audit regulators	D.1.4.	9	100	0	0	9	100

Source: SPSS output

All the auditing firms indicated that they complied with professional standards and applicable legal and regulatory requirements; operated in a way that promoted audit quality and the reputation of the firm; established policies and procedures for complying with applicable legal and regulatory requirements; established policies and procedures for individuals signing audit reports to comply with applicable standards; established policies and procedures for the reliance on work performed by other auditors, whether from the same network or otherwise; and took action to address areas of concern identified by audit regulators in relation to the firm's audit work. Only seven of the firms stated how the audit firm applied policies and procedures to manage potential and actual conflicts of interest.

Table 6.25 illustrates the expert opinion of the CEOs on the operations provisions.

Expert opinions

Table 6.25 Operations of the INEDs on the oversight board

Should the INEDs of the oversight board:	Ref to UK Code	Yes	%	No	%	Total	Total %
Be involved in reviewing people management policies and procedures to protect the public interest?	D.3.2.	8	88.90	1	11.10	9	100

Source: SPSS output

As shown in Table 6.25, eight CEOs agreed that INEDs on the oversight board should be involved in reviewing the policies and procedures to protect the public interest.

Deductions

From the above findings, the application of the operations principle and provisions was good. Even though some firms indicated that they were applying the provisions to a lesser extent, there was nonetheless some form of application. This could be improved with more structured guidelines, explaining what should be practised in the auditing firms. The two provisions that were not applied as desired dealt with the INEDs. The reason for the weak application of these provisions could be directly linked to the lack of INEDs in the auditing firms. It could therefore be argued that application would improve once more INEDs were appointed to the auditing firms.

6.3.5 Reporting

Objective

The objective of these questions was to determine whether the auditing firms applied the reporting principle as contained in the UK Audit Firm Governance Code.

Findings

Table 6.26 Reporting of risks

Application in the firm	Ref to UK Code	To a large extent	To a lesser extent	Totally ineffective	Total	Total %
Describing the risks and explaining how they are being managed or mitigated?	E.3.1.	7	2	0	9	100

Source: SPSS output

Table 6.26 indicates that seven auditing firms carried out a robust assessment of the principal risks the firm was faced with, described the risks and explained how they were being mitigated. Two firms indicated that they did this to a lesser extent.

Table 6.27 Application of reporting principle in auditing firms

Application in the firm	Ref to UK Code	Yes	%	No	%	Total	Total %
Supplies information in a timely manner	E.1.	9	100	0	0	9	100
Supplies quality information	E.1.	9	100	0	0	9	100
Includes a commentary on the firm's performance, position and prospects	E.3.	6	66.70	3	33.30	9	100
Includes fair and balanced information	E.3.2.	7	77.80	2	22.20	9	100
Explains everything in an understandable manner	E.3.2.	7	77.80	2	22.20	9	100
Has an audit committee	E.4.1.	3	33.30	6	66.70	9	100
Has an audit committee which monitors the quality of external reporting	E.4.	3	33.30	6	66.70	9	100
Audit committee maintains relationship with firm's auditors	E.4.	3	33.30	6	66.70	9	100
Discloses on website the audit committee's membership details	E.4.1.	1	11.10	8	88.90	9	100
Has terms of reference for the audit committee	E.4.1.	3	33.30	6	66.70	9	100
Publishes how the audit committee discharge its duties	E.4.1.	2	22.20	7	77.80	9	100
Publishes audited financial statements	E.5.	6	66.70	3	33.30	9	100
Publishes audited financial statements prepared with the financial reporting framework	E.5.	6	66.70	3	33.30	9	100
Publishes audited financial statements that are clear and concise	E.5.	6	66.70	3	33.30	9	100
Explains who is responsible for preparing the financial statements	E.5.1.	9	100	0	0	9	100
Auditors make a statement about their reporting responsibilities	E.5.1.	7	77.80	2	22.20	9	100
States whether the firm adopts the going concern basis and identifies material uncertainties	E.5.2.	9	100	0	0	9	100

Source: SPSS output

Table 6.27 shows the current practice of the reporting principle in the auditing firms. It can be seen that all the firms supplied members of its governance structures, including owners and INEDs, with information in a timely manner and with quality information to enable them to discharge their duties. It can be seen that six of the auditing firms included a commentary on the firm's performance, position and prospects, seven included fair and balanced information and conveyed information in an understandable manner in the transparency report.

Only three of the firms appointed an audit committee while six did not have an audit committee. The three auditing firms that did have an audit committee indicated that it monitored the quality of external reporting and maintained an appropriate relationship with the firm's auditors. All three firms had terms of reference for their audit committee. Only one firm disclosed its audit committee membership details on the company website. Two firms published a description of how the audit committee discharged its duties on an annual basis.

The CEOs of the auditing firms made the following comments:

"We don't have independent non-executive members on the audit committee yet."

"We operate in a partnership model and not that of a public company. The Board structure allows for the functions of audit committee."

"The internal finance committee plays role of audit committee as well."

Six auditing firms indicated that they published audited financial statements that were prepared in accordance with the recognised financial reporting framework, believing these to be clear and concise. All auditing firms explained who is responsible for preparing the financial statements. Seven of the firms indicated that auditors made a statement about their reporting responsibilities, in accordance with the extended audit report standards. All the auditing firms stated whether it was appropriate to adopt the going concern basis of accounting and identified any material uncertainties in its ability to continue to do so, with supporting assumptions or qualifications as necessary.

The CEOs of the auditing firms made the following comments:

"The Annual Financial Statements are part of our Integrated Report."

"The firm is not a public company but a partnership. Financial statements are audited."

"We produce audited financial statements in South Africa, but they are not published locally. We do publish consolidated audited AFS for the global firm."

"Circulation of audited financial statements is limited to internal and business associates including banks it's not for general public."

Deductions

From the findings above, the provisions that were most concerning were those dealing with the audit committee. Only three of the auditing firms had appointed audit committees. From the responses given by the CEOs, it can be seen that some of the firms delegated the audit committee responsibilities and duties to the board or other committees in the firm. It is possible that the auditing firms do not understand the purpose and value that an audit committee can add to the firm.

6.3.6 Dialogue

Objective

The objective of these questions was to obtain the expert opinions of the CEOs on the dialogue principle as contained in the UK Audit Firm Governance Code.

Findings

Table 6.28 Dialogue by the oversight board

Should the oversight board (have):	Ref to UK Code	Yes	%	No	%	Total	Total %
Dialogue with listed company shareholders about corporate governance matters	F.1.	5	55.6	4	44.4	9	100
Enhance mutual communication and understanding with shareholders	F.1.	9	100	0	0	9	100
Disclose policies and procedures for dialogue with listed company shareholders and listed companies?	F.1.1.	4	44.4	5	55.60	9	100
Report on the dialogue the audit firm had during the year?	F.1.1.	6	66.70	3	33.30	9	100
Disclose the nature and extent of the involvement of INEDs in the dialogue?	F.1.1.	4	44.4	5	55.60	9	100
Dialogue with shareholders to enhance mutual communication and understanding?	F.2.	7	77.80	2	22.20	9	100
Dialogue about process of appointment and re-appointment of auditors	F.3.	7	77.80	2	22.20	9	100

Source: SPSS output

Table 6.28 presents the principles that the CEOs felt were most relevant for the oversight board and stakeholder inclusivity. Five of the CEOs believed that the oversight board should have dialogue with listed company shareholders about corporate governance matters. Four CEOs did not agree with this principle. All CEOs believed that the oversight board should enhance mutual communication and understanding to ensure that the audit firm kept in touch with shareholder opinion, issues and concerns. Only four of the CEOs believed that their policies and procedures for dialogue with listed company shareholders and listed companies should be disclosed on their website. However, six CEOs believed that the oversight board should report on the dialogue which the audit firm had during the year. Only four CEOs believed that the oversight board should disclose the nature and extent of the involvement of the INEDs in that dialogue. Lastly, seven CEOs believed that the oversight board should have dialogue with shareholders to enhance mutual communication and understanding as well as having dialogue with listed companies on the appointment and re-appointment of auditors and making considered use of votes in relation to such recommendations.

The CEOs of the auditing firms made the following comments:

> "Our firm is in regular contact with the ARC's of both listed clients and listed targets of the firm with regard to a variety of matters related to quality, partner performance, firm capacity, resources and the like. It is not often that we engage with shareholders of listed clients."
>
> "As Auditing firms we are bound by Independent rules and the terms of reference of the Independent members of Audit Quality Board have to be in line with our Independence obligations."
>
> "We think engagement on matters of audit firm governance would be best directed at the audit committees of listed companies, rather than shareholders."
>
> "It may not be practical to engage with shareholders as firm representative. Discussions with shareholders best handled at institutional levels."

Deductions

The findings on the dialogue principle reveal that not all the auditing firms were in agreement. Although the auditing firms agreed that mutual communication and understanding with shareholders was important, not all concurred that policies and procedures should be disclosed and that the nature and extent of INEDs' involvement in the dialogue should be disclosed.

It is important that the auditing firms understand the value that such provisions would add to the users of the reports and the meaningful information that would be provided to the public, rather than seeing the reporting simply as an obligation. According to the IRBA (2018), auditing firms are required to release transparency reports that provide information on certain elements of the firm and its operations. It is submitted that specific guidelines on the above provisions would assist the firms in reporting in a consistent and complete manner, and that such guidelines would also explain the importance of reporting on dialogue to the auditing firms.

Sections 6.3.7 to 6.3.12 discuss additional questions that were posed in the questionnaire which fell outside the principles and provisions of the UK Audit Firm Governance Code. These questions sought the expert opinion of the CEOs on a South African Audit Firm Governance Code, should one be developed in the near future, as well as any concerns that should be taken into account when drafting such a code.

6.3.7 'Apply and explain' basis framework for South Africa

Objective

The objective of this question was to determine if the CEOs of the auditing firms believed that an 'apply and explain' basis framework would be best-suited for South African auditing firms.

Findings

Table 6.29 Apply and explain framework

	Yes	%	No	%	Total	Total %
Apply and explain framework	7	77.80	2	22.20	9	100

Source: CEO questionnaire (SPSS output)

Table 6.29 indicates that seven CEOs believed that an 'apply and explain' basis would be the most appropriate approach for an Audit Firm Governance Framework for South African auditing firms.

The CEOs made the following comments on the above question:

"The information published in the Transparency Reports of those firms who have published such a report vary significantly, suggesting that Governance Frameworks are equally varied. A consistent approach would allow direct comparisons to be made which would hopefully contribute to reduced market concentration as decision makers became more familiar with structures in place outside of the Big 4."

"Apply and explain promote [sic] transparency overall."

"This will enhance quality of reporting."

"Akin to the King IV Report."

"This will ensure that firms are transparent and provide the reasons where there [sic] in non-compliance."

"We believe the better approach would be rules-based. The differences in size and resources among the firms are too big and resource limitations could easily be used as an excuse for not fully applying many of the principles."

"Each firm is unique."

Literature and deductions

According to the literature review, King IV applies the 'apply and explain' basis. The 16 principles can be adopted by any company and it is necessary to substantiate the practice of corporate governance (IoDSA, 2016). The required explanation gives effect to each principle and enables stakeholders to make an informed decision on whether a company is well governed or not. The explanation also helps in shifting the focus of companies from a compliance mindset to a qualitative mindset, which encourages the achievement of objectives through careful consideration of the entity's circumstances (IoDSA, 2016; Piek, 2016).

From the above discussion, it can be deduced that the majority of the auditing firms believe that an 'apply and explain' basis would be the most appropriate approach for auditing firms in South Africa. This is in line with the basis used in King IV, thus confirming that a sector supplement in future King developments would be acceptable to most of the large and medium-sized auditing firms.

6.3.8 Difficulties in implementing an audit firm governance framework in South Africa

Objective

The objective of this question was to determine the difficulties with implementing an Audit Firm Governance Framework in South Africa, as expressed by the CEOs of the top nine auditing firms in South Africa.

Findings

The CEOs made the following comments on the above question:

"Lack of resources in firms outside the Big 4. In particular financial resources where the cost of audit quality has eroded profits. There may still be a large proportion of partners who believe in a partnership model rather than a corporate model and believe these governance structures are an overkill for a professional firm, which is run by the shareholders on a day to day basis."

"Auditing firms are largely privately owned entities despite the fact that they may have a public interest mandate."

"Limited pool of independent non-executive directors as well conflict of interest."

"Global Firm Management Structures will introduce certain limitations."

"The Auditing Profession Act. 2005 needs amendment as it does not allow for Independence. All Directors/Partners must be shareholders of the firm."

"None. It will however be a lot more of a conducive environment if the regulator institutes a limited liability regime in line with most jurisdictions in the world."

"Resources available to small and medium firms. The initial framework must be simple enough for any firm to implement and can be expanded on in the future. If transformation is to be considered in the composition of the governance structure, then the availability of willing experienced directors may be a challenge."

"The complexities of structures of various firms, especially the concept of multidisciplinary practices not recognised by regulators."

"The cost and the burden of further compliance that would increase costs to the client and ultimately to the consumers."

Literature and deductions

The literature review in Chapter 4 discussed the concerns about corporate governance in auditing firms, namely, (i) the lack of a specific corporate governance code for auditing firms, (ii) how to determine the independence of a director appointed to an audit firm board and (iii) the lack of independence on oversight boards that have been implemented at some auditing firms, (iv) legislation such as the APA that prevent auditing firms from appointing INEDs to their EXCO. It was also highlighted that even though most large auditing firms have oversight boards, there was still very little independence on these boards.

The above comments once again reflect the contradicting opinions of the various CEOs in the population. Some CEOs believed that there would be no difficulties in implementing such code while other (possibly smaller) auditing firms believed that it would result in a financial burden on the firms. An important point was also made by one of the CEOs (which is also supported in the literature review). The CEO stated that the APA would have to be amended to allow for the appointment of INEDs in auditing firms. These are all valid concerns, but not concerns that should completely stop the implementation and practice of corporate governance within auditing firms.

6.3.9 Appointment of an oversight board

Objective

This question sought to establish whether the CEOs of the auditing firms believed that the auditing firms needed to appoint an oversight board which would be responsible for the corporate governance of the audit firm in order to properly fulfil their public interest responsibilities.

Findings

Table 6.30 Appointment of oversight board

	Yes	%	No	%	Total	Total %
Appointment of an oversight board	8	88.90	1	11.10	9	100

Source: CEO questionnaire (SPSS output)

Table 6.30 indicates that eight of the auditing firms believed that it was necessary to appoint an oversight board which would be responsible for the corporate governance of the firm, in order to properly fulfil their public interest responsibilities.

Below are comments made by the CEOs on the above question.

"The public interest and resulting perception of auditing firms has increased significantly and auditors cannot be blind to responding appropriately in order to regain the public confidence. If greater transparency and improved governance leads to this, the profession will be in a better place."

"Audit firm leadership are the custodians of the firm and as such are responsible for discharging their public interest responsibilities."

"The oversight board will bring a perspective that is independent from that of executive board members. They will also be valuable in educating the public on the role of auditors because currently anything that goes wrong in a company the blame lies with auditors."

"Audit Quality Board focused on the Audit Practice."

"Evident from the Brydon review in the UK and new FRC principles."

"The independent members would ensure that the firm serves public interest."

"Auditing firms are for profit organisations. Independent oversight is needed to ensure that the profit motive does not overshadow public interest responsibility."

Literature and deductions

The FRC (2010) states that the appointment of INEDs to auditing firms indicates that regulation is not a replacement for effective governance but rather, that good governance supplements regulation in the promotion of audit quality. At present, the corporate structures of auditing firms are flawed. Some auditing firms argue that they need not comply with the codes of corporate governance as their business model is based on a 'partnership' (Aberian, 2019). According to Nkuhlu (2020), all auditing firms need to appoint INEDs and place risk and ethics under their oversight.

The above findings illustrate that the majority of the CEOs of the auditing firms agree that the appointment of an independent oversight board would assist in restoring public interest in the profession. This is in line with the literature, which states that there is a need for independent oversight in auditing firms.

6.3.10 Audit vs non-audit part of auditing firms

Objective

The objective of this question was to determine if the CEOs believed that the corporate governance framework should distinguish between the audit and non-audit parts of auditing firms.

Findings

Table 6.31 Frameworks for audit and non-audit parts

	Yes	%	No	%	Total	Total %
Different framework for audit and non-audit	6	66.70	3	33.30	9	100

Source: CEO questionnaire (SPSS output)

From Table 6.31, it is evident that six of the CEOs believed that there should be different frameworks for the audit and non-audit parts of the auditing firms.

Below are some of the comments made by the CEOs on this question:

"Our experience is that the individuals offering advisory services often have different drivers and as a result may need to have different governance in place. Examples of this are earnings models for Advisory divisions and in some cases a reduced focus on conflicts of interest, independence etc."

"The code of ethics, quality standards, all policies and procedures are to be complied with by all within the audit firm."

"The Audit Practice is Regulated whereas other parts of the business are not."

"The focus is on audit quality."

"There's a perception that firms are more focused on consulting and its profit than on the public interest function and the focus will go a long way in mitigating the situation."

"Having different rules and processes might confuse the organisation."

Deductions

From the above comments, it is clear that there are conflicting views and opinions from the CEOs. However, it appears that the majority of the CEOs believes that two different frameworks will not be necessary.

6.3.11 Key areas in terms of governance

Objective

This question sought to identify the areas that the CEOs believed should be addressed to ensure that the public interest was protected.

Findings

Below are the answers to the open-ended question which were posed to the CEOs. Quality and ethics seem to be the main factors identified.

"Independence, conflict of interest, quality, ethics and external stakeholder communication."

"Leadership, Audit Quality, Risk Management."

"Audit quality, risk management, conflict of interest, corporate governance matters, control environment and regulatory matters."

"Audit Quality Management, Independence, Ethics, Culture, Audit Quality Indicators."

"Audit quality."

"Audit quality and ethics."

"The areas in line with King IV, adapted for auditing firms, i.e. more focus on quality, ethics and focus on public interest."

"Auditor independence, due to its impact on audit quality."

"Quality audits and total independence and through audits."

Literature and deductions

According to the Institute on Governance (2020), governance consists of the following principles, which also frequently recur in much of the literature. These include legitimacy and voice, direction, performance, accountability and fairness. In Chapter 1, the definition of corporate governance was formulated as:

> *A set of responsibilities and practices instituted by the governing body in order to direct a company to achieve its strategic objectives while remaining sustainable, accountable and transparent and acting in the best interest of all the stakeholders.*

Based on the comments from the CEOs and the definitions on corporate governance in the literature, the auditing firms seem to be in agreement that the most important areas that should be focused on include independence, managing conflicts of interest, ethics, leadership and audit quality. These areas would be specifically applicable to auditing firms, and emphasise the need for a code or guidelines particularly designed for auditing firms.

6.3.12 Additional comments in questionnaire to assist the study

The CEOs were also asked to provide any additional comments on the study, as indicated below:

"Audit rotation and transformation should be handled with caution to avoid any further failures and disappointments in the profession."

"The responses related to governance are in the context of the nature of our organisation i.e. ownership structure and regulatory environment. As an example, the King Code may not be applicable in its entirety but certain elements can be adopted. It is important to factor that in assessing the most appropriate governance structure."

"Governance structures should align with ISQM 1 principles and should not be prescriptive."

"Auditing firms have a small window to rebuild public trust. They need to address all the criticism that are [sic] levelled against them seriously if the profession is to survive."

From the above comments, it is clear that the CEOs concur that public trust should be restored in the audit profession, but that this should be carefully thought through and done with caution. It is also evident that a specific code for auditing firms should be developed, which is aligned with the current audit regulations and legislation. This is because King IV, as it currently stands, will not be applicable to auditing firms in its entirety. This finding supports the objective of the study, which calls for a sector supplement for auditing firms to be included in future iterations of the King Code.

6.3.13 Conclusion

Section 6.3 explained in detail the quantitative findings from the questionnaires that were sent to the CEOs of the top nine auditing firms in South Africa. The findings were categorised according to the six principles contained in the UK Audit Firm Governance Code. The application of the principles and provisions in the auditing firms was examined and the expert opinions of the CEOs were provided thereafter. Reference was made to the literature supporting each finding, followed by deductions at the end of each principle. The findings on the additional questions included in the questionnaire were also discussed and the expert opinions of the CEOs were provided.

The development of an Audit Firm Governance Code for South African auditing firms is critical for the effective application and disclosure of corporate governance principles in South African auditing firms. The CEOs of the auditing firms are highly qualified professionals, with high standing and impeccable character; as such, their expert views on this topical problem are held in high regard. The questionnaire completed by them provided valuable information on their current corporate governance structures as well as their views and opinion on the development of a corporate governance framework for auditing firms in South Africa.

From the information obtained via the questionnaire, it is evident that corporate governance plays a key role in auditing firms; the firms also understand the importance of good corporate governance. However, South African auditing firms are facing serious challenges, such as finding members who are independent, have the relevant skills, experience and competence and who are prepared to serve on an oversight board of an audit firm. Some of the firms also indicated that limited financial resources would prevent them from implementing strict corporate governance guidelines.

The following concluding remarks from the respondents reflect the high standing and importance of corporate governance, the challenges it faces and the value of this research.

Why a corporate governance code is necessary and supported:

"The presence of independent members heightens awareness on others members of their custodianship of good governance."

"The oversight board can be valuable also in helping with restoring trust in the entire profession."

"Apply and explain promote transparency overall and will enhance the quality of reporting."

"We believe the better approach would be rules-based. The differences in size and resources among the firms are too big and resource limitations could easily be used as an excuse for not fully applying many of the principles."

"The public interest and resulting perception of auditing firms has increased significantly and auditors cannot be blind to responding appropriately in order to regain the public confidence. If greater transparency and improved governance leads to this, the profession will be in a better place."

"The oversight board will bring a perspective that is independent from that of executive board members. They will also be valuable in educating the public on the role of auditors because currently anything that goes wrong in a company the blame lies with auditors."

"The independent members would ensure that the firm serves public interest."

“Auditing firms are for profit organisations. Independent oversight is needed to ensure that the profit motive does not overshadow public interest responsibility.”

“Auditing firms have a small window to rebuild public trust. They need to address all the criticism that are levelled against them seriously if the profession is to survive.”

Why a corporate governance code could be challenging:

“The questions suggest that non-execs should be appointed to appropriate Boards. We have had this previously but IRBA were not in support of it.”

“Our firm does not have any independent non-executive directors.”

“We operate in a partnership model and not that of a public company.”

“Our experience is that additional layers of governance which may duplicate responsibilities will squeeze profitability even further, resulting in the auditing profession continuing to be an unattractive option for new entrants.”

“We currently do not have a legal framework for an oversight board.”

“King IV might not be entirely applicable to audit firm environment and structure.”

“The information published in the Transparency Reports of those firms which have published such a report vary significantly, suggesting that Governance Frameworks are equally varied. A consistent approach would allow direct comparisons to be made which would hopefully contribute to reduced market concentration as decision makers became more familiar with structures in place outside of the Big 4.”

“Lack of resources in firms outside the Big 4. In particular financial resources where the cost of audit quality has eroded profits. There may still be a large proportion of partners who believe in a partnership model rather than a corporate model and believe these governance structures are an overkill for a professional firm, which is run by the shareholders on a day to day basis.”

“Auditing firms are largely privately owned entities despite the fact that they may have a public interest mandate.”

“Limited pool of independent non-executive directors as well conflict of interest.”

"The Auditing Profession Act 2005 needs amendment as it does not allow for independence. All directors/partners must be shareholders of the firm."

"Resources available to small and medium firms. The initial framework must be simple enough for any firm to implement and can be expanded on in the future. If transformation is to be considered in the composition of the governance structure, then the availability of willing experienced directors may be a challenge."

"The complexities of structures of various firms, especially the concept of multidisciplinary practices not recognised by regulators."

6.4 Points of triangulation

In Chapter 5, it was explained that a data transformation triangulation model (Creswell, 2003) was adopted in this study. Section 6.2 provided a qualitative analysis of the transparency reports of the top nine auditing firms in South Africa. The findings were then transformed into frequency counts (Creswell, 2003), which quantified the data. Selected data from the frequency counts is now compared with the CEO questionnaire feedback from the top nine auditing firms in South Africa. The objective is to triangulate the data collected from the content analysis of the transparency reports with the responses received from the CEOs. This is done to validate, compare and interrelate the corporate governance applied and disclosed in auditing firms in South Africa.

The triangulation is presented according to the six principles contained in the UK Audit Firm Governance Code.

6.4.1 Leadership

Table 6.32 Triangulation: Reports published

		Content Analysis		Questionnaire	
	Ref to UK Code	Yes	No	Yes	No
Transparency report	A.1.2.	7	2	7	2
Integrated report	A.1.2.	2	7	3	6

Source: SPSS calculation, own comparison.

As can be seen in Table 6.32, the above triangulation presents a perfect correlation between the content analysis and the questionnaire. This is also a confirmation that all the published transparency reports were included in the content analysis, which was conducted for the qualitative research. It also confirms that the seven auditing firms that published transparency reports made it relatively easy to obtain the reports. The transparency reports which were available on the websites were easier to obtain than the ones which had to be requested from the auditing firms themselves via email. One recommendation would for all transparency reports to be publicly available on the auditing firms' website.

With reference to the integrated reports, there was a slight difference in the findings. The researcher was able to obtain only two integrated reports from the auditing firms. A search of the websites of the other auditing firms revealed no integrated report. Consequently, a personal email was sent to each audit firm requesting their integrated report. No auditing firms responded to this request. It could be argued that the email was not delivered to the relevant person and therefore, hence the discrepancy in the findings.

It can therefore be concluded that the two types of reports could be combined and, with the assistance of corporate governance guidelines or a formal code, the auditing firms could disclose information consistently and understand clearly what was expected of them. This would also minimise the duplication of information in two separate reports.

Table 6.33 Triangulation: Governance structure disclosures

		Content Analysis		**Questionnaire**	
	Ref to UK Code	**Yes**	**No**	**Yes**	**No**
EXCO information disclosed in transparency report.	A.1.1.	7	0	9	0
Oversight board information disclosed in transparency report.	A.1.1.	2	5	7	2

Source: SPSS calculation, own comparison.

As can be seen in Table 6.33, only seven of the auditing firms disclosed that they had an EXCO, whereas in actual fact, all the auditing firms had an EXCO. This discrepancy is due to the fact that two of the auditing firms did not issue a transparency report. It is rather concerning that only two of the auditing firms disclosed information about a South African oversight board in their transparency report, when it was indicated through the questionnaire that seven of the firms actually had a South African oversight board. It appears that these firms are not making use of a valuable opportunity to communicate important governance oversight structures and practices to their stakeholders.

Table 6.34: Triangulation: Leadership with reference to the EXCO

		Content Analysis		Questionnaire	
Is the following disclosed in the transparency report about the EXCO?	**Ref to UK Code**	**Yes**	**No**	**Yes**	**No**
Duties	A.1.2.	2	5	8	1
Decisions	A.1.2.	1	6	8	1
Job titles	A.1.3.	3	4	9	0
Election and appointment	A.1.3.	1	6	9	0
Terms	A.1.3.	1	6	8	1
Length of service	A.1.3.	2	5	8	1
Meeting attendance	A.1.3.	0	7	8	1
Biographical details	A.1.3.	0	7	9	0

Source: SPSS calculation, own comparison.

As shown in Table 6.34, the auditing firms did not disclose the necessary information about their EXCO. From the questionnaires, the CEOs provided their expert opinions on the above provisions, with the majority of the firms believing that the disclosure of information about the EXCO was important. The lack of disclosure in the transparency reports could be due to the fact there is currently no code to guide the auditing firms on the information that should be disclosed.

Table 6.35: Triangulation: Leadership with reference to the oversight board

		Content Analysis		Questionnaire	
Is the following disclosed in the transparency report about the oversight board?	**Ref to UK Code**	**Yes**	**No**	**Yes**	**No**
Duties	A.1.2.	2	5	8	1
Decisions	A.1.2.	2	5	8	1
Job titles	A.1.3.	3	4	9	0
Election and appointment	A.1.3.	1	6	9	0
Terms	A.1.3.	1	6	8	1
Length of service	A.1.3.	2	5	8	1
Meeting attendance	A.1.3.	1	6	8	1
Biographical details	A.1.3.	1	6	9	0

Source: SPSS calculation, own comparison.

Table 6.35 presents once again a variance between the qualitative and the quantitative findings. The qualitative findings state that very few auditing firms disclose the above information in their transparency reports with reference to their oversight boards. This is obviously also due to lack of oversight boards within auditing firms. It is, however, pleasing to note that at least eight (and in some cases more) of the auditing firms believed that these principles were very important and that the stated information should be disclosed about the members of the oversight board. This is a positive outcome and already a step in the right direction since it shows that the CEOs of understood the importance of disclosing such information to the public about their oversight board.

6.4.2 Values

Table 6.36 Triangulation: Values

		Content Analysis		**Questionnaire**	
	Ref to UK Code	**Yes**	**No**	**Yes**	**No**
Code of conduct on website	B.1.3.	5	2	6	3
Discloses on the website to whom the code of conduct is applicable	B.1.3.	5	2	6	3

Source: SPSS calculation, own comparison.

As can be seen in Table 6.36, five of the auditing firms disclosed their codes of conduct on their website as well as to whom the code of conduct was applicable. Six of the firms stated that they disclosed such information. However, there was a slight difference between the content analysis and the questionnaire. In providing additional comments, one of the firms indicated that their code of conduct was disclosed in their 'Clarity Charter'. The researcher was not aware of this and regarded it as non-disclosure. It was, however, subsequently confirmed by the researcher that the audit firm's code of conduct was included in the 'Clarity Charter' and therefore the qualitative and quantitative findings correlated with one another.

Below is a comment provided by the CEO:

"Our audit firm has launched our Clarity Charter which is a purpose statement setting out our approach to values, ethics and quality. It contains much of what could be found in a Code of Conduct."

6.4.3 INEDs

Table 6.37 Triangulation: INEDs on the oversight board

		Content Analysis		Questionnaire	
	Ref to UK Code	Yes	No	Yes	No
Consists of majority of INEDs?	C.1.1.	0	7	1	8
Has at least three INEDs?	C.1.1.	2	5	3	6
Discloses reasons for not having at least three INEDs?	C.1.1.	0	7	8	1
Has a majority of INEDs who are members of other relevant governance structures in the firm?	C.1.1.	2	5	3	6
Disclose: Appointment, retirement and resignation of INEDs	C.1.2.	1	6	8	1
Disclose: Remuneration of INEDs	C.1.2.	1	6	7	2
Disclose: Duties of INEDs	C.1.2.	1	6	8	1
Disclose: INEDs discharge of duties	C.1.2.	1	6	8	1
Disclose: Firm support for INEDs	C.1.2.	1	6	9	0
Disclose: How the firm positions INEDs	C.1.2.	3	4	8	1
Has INEDs who have skills and experience in audit	C.2.	2	5	8	1
Has INEDs who are competent in auditing/accounting	C.2.1.	2	5	8	1
Disclose: INEDs' impact on independence	C.2.1.	1	6	9	0
Discloses on its website procedures for dealing with any fundamental disagreement	C.3.6.	0	7	1	8

Source: SPSS calculation, own comparison

As shown in Table 6.37, there were very large discrepancies between the content analysis and the questionnaires. The content analysis found that only one audit firm disclosed the information on the appointment, retirement, resignation, remuneration and duties of INEDs, the manner in which the INEDs discharged their duties and how the audit firm supported the INEDs in discharging their duties. From the CEOs' opinions, it emerged that more than seven of the auditing firms regarded these principles as important to be disclosed in the transparency reports. The obvious reason for this variance was the lack of INEDs appointed to auditing firms, and clearly, if the firms did not have INEDs, they would not be able to disclose such information. However, it was concerning to note that although the CEOs admitted the importance of the disclosure of such information, they did not apply the principles.

Three of the auditing firms disclosed how they positioned their INEDs (on the EXCO or the oversight board) and eight CEOs regarded this as important information to disclose in the transparency report.

Only one of the auditing firms disclosed the criteria for assessing the impact of INEDs on the firms' independence as auditors and their independence from the firm and its owners, yet all of the CEOs agreed that this was an important principle to disclose in the transparency report.

From the above, it can be deduced that the CEOs understood the importance of appointing INEDs and the disclosure of information about the INEDs in the transparency report. The real challenge came with the implementation of these principles and the appointment of the INEDs in the auditing firms.

As can be seen in Table 6.37, only two of the auditing firms disclosed that they have at least three INEDs on their oversight board, as well as INEDs that were part of other governance structures and who had the relevant skills and experience in audit and were competent in auditing and/or accounting. Only three of the CEOs thought it was important to have at least three INEDs on the oversight board as well as INEDs who were part of other structures of the audit firm. The divergence in opinions and the higher negative opinions could be due to the fact that there are difficulties in appointing so many INEDs within auditing firms. Eight of the CEOs believed that the skills, experience and competence of the INEDs in accounting and auditing were important. None of the firms disclosed reasons for not having at least three INEDs on their oversight board, yet eight of the CEOs regarded this as an important provision.

None of the auditing firms had an oversight board with a majority of INEDs. Only one CEO found this to be important whereas the remainder believed it was not necessary. This could be directly linked to the fact that it is difficult to appoint INEDs who are totally independent from the auditing firms.

The content analysis revealed that none of the auditing firms disclosed on their website the procedures for dealing with fundamental disagreements between INEDs and members of the firm's management team and/or governance structures. This is clearly linked to the fact that only three of the firms had appointed INEDs. The CEOs' responses indicated that one audit firm disclosed this information while the remaining eight did not. However, the one firm that disclosed this information stated that it did so somewhere on its website, in a document which was not easily accessible to the public.

6.4.4 Operations

Table 6.38 Triangulation: Operations

		Content Analysis		Questionnaire	
	Ref to UK Code	**Yes**	**No**	**Yes**	**No**
Policies and procedures to manage conflicts of interest	D.1.3.	4	3	7	2
Disclosure: Effectiveness of the internal control system	D.2.2.	2	5	6	3
Disclosure: Weaknesses in internal control system	D.2.2.	2	5	6	3
Disclosure: Actions to deal with weaknesses	D.2.2.	2	5	6	3
Disclosure: How the firm supports its commitment to professionalism, openness and risk management	D.3.	1	6	8	1
Disclosure: Whistleblowing policies and procedures	D.4.	6	1	8	1

Source: SPSS calculation, own comparison

The content analysis revealed that four of auditing firms indicated how the firm applied policies and procedures for managing potential and actual conflicts of interest. The questionnaire findings stated that seven of the auditing firms indicate how the firm applied policies and procedures for managing potential and actual conflicts of interest.

Table 6.38 indicates the variances between the qualitative and quantitative findings. Very few auditing firms two disclosed information about their internal controls and their effectiveness, any identified weaknesses, and actions taken to address those weaknesses. In contrast, six of CEOs stated that their auditing firms disclosed this information in their transparency reports.

There was a large discrepancy between the disclosure on the auditing firms' websites on how the firms supported their commitment to professionalism, openness and risk management. Only one firm disclosed such information clearly on its website, yet eight of the firms stated that they did disclose this on their websites. The qualitative study found that only six of the auditing firms disclosed their whistleblowing policies and procedures, yet eight of the CEOs stated that their auditing firms did disclose these policies and procedures.

6.4.5 Reporting

Table 6.39 Triangulation: Reporting

		Content Analysis		Questionnaire	
	Ref to UK Code	Yes	No	Yes	No
Includes a commentary on the firm's performance, position and prospects	E.3.	3	4	6	3
Includes fair and balanced information	E.3.2.	4	3	7	2
Explains everything in an understandable manner	E.3.2.	6	1	7	2
Has an audit committee	E.4.1.	3	4	3	6
Publishes audited financial statements	E.5.	0	7	6	3
Publishes audited financial statements prepared with the financial reporting framework	E.5.	0	7	6	3
Publishes audited financial statements that are clear and concise	E.5.	0	7	6	3
Explains who is responsible for preparing the financial statements	E.5.1.	0	7	9	0

Source: SPSS calculation, own comparison.

Only three of the auditing firms included commentary on the firm's performance, position and prospects, yet six of firms stated that they did so in their transparency reports.

Only four of the firms included information in their transparency reports that was deemed fair and balanced (as evaluated by the researcher), yet seven of the firms believed that their information was fair and balanced. This finding could be subjective due to different individuals interpreting the reports differently.

There was a smaller difference with regards to the understandability of the information. The content analysis showed that six of the auditing firms explained information in an understandable manner whereas seven of the firms believed that their information was understandable.

Table 6.39 indicates a correlation between the disclosure in the transparency reports and the responses of the CEOs on the existence of audit committees. Only three of the auditing firms had audit committees and only one of these committees was constituted in terms of the principles of King IV.

Table 6.39 presents a significant variation between the findings of the content analysis and the questionnaires completed by the CEOs. The content analysis found no published audited financial statements in the transparency or integrated reports of the auditing firms, yet the six of the CEOs indicated that their firms published audited financial statements. Because no financial statements could be found for any of the auditing firms, the questions relating to the recognised financial reporting framework, clear and concise statements and who was responsible for the preparation of the statements could not be analysed and 'No' answers were recorded for these questions. All of the CEOs stated that they explained who was responsible for the preparation of the financial statements. This could be that they disclosed who prepared the financial statements vaguely in the transparency reports, however, no evidence could be found of such information.

6.4.6 Dialogue

Table 6.40 Triangulation: Dialogue

		Content Analysis		Questionnaire	
	Ref to UK Code	**Yes**	**No**	**Yes**	**No**
Discloses policies and procedures for dialogue with listed company shareholders and listed companies?	F.1.1.	3	4	4	5
Discloses the nature and extent of the involvement of INEDs in the dialogue?	F.1.1.	1	6	4	5

Source: SPSS calculation, own comparison

Table 6.40 indicates that only three of the auditing firms' dialogue policies and procedures could be found on their websites. It could be that the policies were not easily accessible or visible on the websites. The second principle was more concerning, as evidence of the nature and extent of INEDs' involvement in dialogue with shareholders could only be found for one firm, yet four firms stated that they disclosed this information.

These discrepancies could be due to the websites being diverse and information not being easily accessible. It was also found that auditing firms disclosed their information in different documents and reports, making it difficult for the public to access the information easily.

The development of a governance code for auditing firms which specifies where the relevant information should be disclosed would ensure that all auditing firms disclose the same information through the correct platforms.

6.5 Conclusion

This chapter presented the findings of the empirical study. Given the 100% response rate and the professionalism and expertise of the respondents, the information is considered to be representative of the large and medium-sized auditing firms in South Africa.

The results of the empirical study found strong evidence indicating that the current corporate governance practices and disclosures in South African auditing firms lack structure and consistency. The findings of the triangulation revealed discrepancies between the firms' current disclosure in their transparency reports and what is being practised in the firms versus what they consider to be important in terms of corporate governance. Most of the principles mentioned in the questions were strongly supported by the majority of the auditing firms. This is a positive outcome since it validates the need for an Audit Firm Governance Code for South African auditing firms.

Chapter 7 discusses the findings of the study and recommendations are made for improving corporate governance in auditing firms. Areas of future research are also identified.

Chapter 7: CONCLUSION

7.1 Introduction

This chapter concludes the study by describing how the research objectives were met and how the underlying research problem was addressed. Recommendations are formulated based on the results and areas for future research are indicated.

Chapters 1 to 4 contained the literature relevant to this study. This review contributed to the existing body of knowledge and assisted in addressing the research problem. Chapter 6 presented the findings of the empirical research, describing the governance disclosures and practices at auditing firms in South Africa to address the research problem. This chapter provides a detailed explanation of how the research objectives were met.

7.2 Overview of the research objectives

To address the research problem, research objectives were formulated. These were achieved through a comprehensive literature review and empirical study. The transparency reports and integrated reports of large and medium-sized auditing firms in South Africa were analysed. Questionnaires were then sent to the CEOs of the auditing firms and the results were triangulated between the two data sets to compare and validate the data.

The following section discusses how each research objective was met. The discussion is structured according to the six objectives, providing details on how the literature review and the empirical study assisted in achieving the objectives. The empirical study also indicates (where relevant) which specific principles of the UK Audit Firm Governance Code were used to address the objectives. Each section has its own conclusion to summarise the findings.

In Chapter 1 the research problem for the study was defined as follows:

> *Auditing firms in South Africa do not have effective governance structures and are not applying corporate governance practices and principles. This is evident from the amount of corporate scandals and failures that have taken place recently and the auditor implication in these scandals. The current corporate governance code in South Africa, King IV, does not have a*

specific sector supplement for auditing firms. Therefore, this study aims to provide guidelines on corporate governance practices and oversight structures for auditing firms in South Africa which could possibly be included as a sector supplement in future King Code iterations.

This research problem was addressed through the six research objectives, as discussed below.

7.2.1 Research objective 1: Corporate governance developments in the UK, USA, Australia, the Netherlands and more specifically, in South Africa

The aim of this research objective was to conduct a literature review examining the developments in corporate governance in the UK, USA, Australia, the Netherlands and South Africa. This was done to identify the corporate governance codes that have been introduced over the years and to determine which of these could be applied to South African auditing firms. The literature review also aimed to identify any corporate governance codes or legislation that was specifically developed for auditing firms. The literature review went in to examine theories of corporate governance, thereby providing the theoretical framework for the study. The stakeholder theory and the shareholder theory were deemed to be best-suited for the purposes of this study. As discussed in Chapter 2, the stakeholder theory was found to be the most appropriate for the suggested corporate governance guidelines. This theory was incorporated into the design of the checklist and questionnaire used in the study.

The following section outlines the key findings from the literature review that support research objective 1.

Literature findings

i. From the literature study it is evident that corporate governance is not a new concept, developing across the world over the last 40 years. The renewed emphasis on corporate governance can be attributed to the major corporate collapses and business failures taking place in recent years. The auditing profession has been in the news for all the wrong reasons and the lack of corporate governance at auditing firms has been one of the main contributors to these corporate failures where auditing firms have been involved.

ii. Corporate governance is often described in terms of two seemingly opposing models—the shareholder model and the stakeholder model. These two models are also known as one-tier and two-tier board structures. From the literature, it is evident that auditing firms should apply a two-tiered board structure to appoint an independent oversight board. In South Africa, due to limitations created by the APA of 2005, INEDs cannot be appointed as members of the EXCO of auditing firms.

iii. Corporate governance codes arose out of deep-seated concerns stemming from well-publicised corporate failures. With the current corporate failures and scandals on the rise in South Africa, there is an urgent need for a corporate governance code specifically for auditing firms.

iv. The APA provides information on the governance of the regulatory board of the audit profession, such as the IRBA, but not specifically for auditing firms as organisations. ISQC 1 and ISA 220 provide information on the governance and leadership and ethical requirements of auditing firms. This information is, however, very limited, with no detailed guidelines on audit firm governance. The UK's Brydon Report emphasises the principles of corporate auditing and the importance of acting in the public interest. This report, like most other reports, acts or codes, focuses more on the governance of the individual auditor rather than the auditing firm specifically. This shortcoming emphasises the need for a sector supplement specifically for auditing firms.

v. The literature review found that the UK Audit Firm Corporate Governance Code of 2010 (reviewed in 2016) was designed specifically for auditing firms. The Code consists of six principles: (1) leadership, (2) values, (3) independent non-executives, (4) operations, (5) reporting and (6) dialogue. These are the principles which were used in the empirical research of this study. The provisions contained in this Code also informed the design of the checklist and the questionnaire.

vi. The literature found that South Africa has a strong colonial legacy with resultant ties with the UK. As the UK already has a corporate governance code specifically for auditing firms, this code, together with King IV, can be used as the basis to create guidelines on corporate governance practices and oversight structures for auditing firms in South Africa. The UK Code was used in the empirical research of this study to establish the current governance practices and disclosures of auditing firms in South Africa.

The following section discuss how research objective 1 was achieved through the empirical study.

Empirical findings

The empirical study was informed by the findings of the literature review. Thus, the corporate governance codes identified in the literature review, such as the UK Audit Firm Governance Code and King IV, were used as the basis to develop the checklist and the questionnaires. As stated above, due to the strong colonial legacy and resultant ties with the UK, South Africa could make use of the UK Audit Firm Governance Code as the basis for the development of a corporate governance code for South African auditing firms. The findings of the empirical study were thus used to determine the current governance practices and disclosures in South African Auditing firms.

Conclusion for research objective 1:

The literature review found that the UK is the only country with an Audit Firm Governance Code. The principles and provisions of this Code were specifically designed with auditing firms in mind.

This Code was used in the empirical study to develop the checklist and the questionnaire. The empirical research found that the principles contained in the UK Audit Firm Governance Code could easily be applied to South African auditing firms. The triangulation in Chapter 6 indicated that many of the firms believe the principles and provisions in the Code are important and would add value to the auditing firms and all stakeholders. The checklist and the questionnaire found that many of the principles and provisions are already applied in auditing firms in South Africa. However, the application is inconsistent and differs from one firm to the next, depending on firm size and resources. A formal South African code or guidelines would assist auditing firms to adopt the same principles and practices. Consequently, the disclosures of such principles would be more consistent across auditing firms. This finding adds weight to the suggestion that audit firm governance should be included as a sector supplement in future King Code iterations.

7.2.2 Research objective 2: Comparison between the UK Audit Firm Governance Code and King IV to identify corporate governance similarities

The second research objective aimed to identify similarities between the UK Audit Firm Governance Code and King IV. This comparison determined whether the principles contained in the UK Code were more or less in line with those contained in King IV. It was postulated that, should the principles between the two codes be similar, it would be easier for South African auditing firms to apply and accept a corporate governance code for auditing firms. This is because the firms were already familiar with King IV and had already implemented some of its principles, albeit only to a very limited extent. The UK Audit Firm Code was first introduced in 2010, thus, the UK has already experienced and eliminated most of the teething issues that one would expect following the introduction of a new code. As stated earlier, the Cadbury Report was used as the basis for the development of the King Code. Consequently, the UK Audit Firm Governance Code could, in turn, be used as the basis for the development of a South African audit firm governance code.

The key findings of the literature study are outlined below.

Literature findings

The comparison between the UK Audit Firm Governance Code and King IV (see Annexure I and Chapter 2) indicate that the majority of the principles and provisions contained in the UK Code are also found in King IV. This means that King IV as it currently stands, already contains principles that could easily be implemented in auditing firms in South Africa. A sector supplement for auditing firms would be an ideal addition to future King Code iterations. A summary of the comparison is provided below.

Table 7.1: Comparison between the UK Audit Firm Governance Code Principles and King IV principles

UK Audit Firm Governance Code Principles	KING IV principles that address the same principle as the UK Code
Leadership	Principles 6, 7, 9 and 10
Values	Principles 1, 2, 16
Independent non-executives	Principle 7
Operations	Focuses on auditing firms, thus not applicable in King IV
Risk Management	Principle 11
Reporting	Principles 5, 11, 8
Dialogue	Principle 16

Source: Researcher's own comparison

The following section discusses how research objective 2 was achieved through the empirical study.

Empirical findings

The disclosure in the transparency reports of the auditing firms, as identified through the content analysis, revealed that South African auditing firms are already applying some of the principles contained in the UK Code and thus indirectly in King IV. However, this disclosure between the firms is inconsistent, although as stated, this could largely be due to the lack of guidelines for auditing firms on corporate governance practices and disclosures. The empirical study requested the expert opinions of the CEOs of the auditing firms about the implementation of the UK principles. The findings indicated that the majority of the CEOs believe that the principles contained in the UK Code should be implemented in South African auditing firms. One of the CEOs stated that there are no difficulties in implementing King IV in South African auditing firms. This finding supports the above comparison from the literature review, namely, that the King IV—with some adjustments for auditing firms—could be applied to auditing firms in South Africa. This also supports the objective that future King iterations should include a sector supplement specifically for auditing firms.

Conclusion for research objective 2:

The literature review identified the principles and provisions contained in the UK Audit Firm Governance Code and King IV. The comparative study found that the majority of the principles contained in the UK Code are already contained in King IV. However, one principle—operations—was specifically designed for auditing firms and is therefore not covered in King IV.

7.2.3 Research objective 3: Financial corporate failures in the UK, USA, Australia, the Netherlands and South Africa and the role of auditing firms in these failures

The aim of this objective was to establish how the lack of corporate governance in auditing firms had contributed to some of the worse financial corporate failures in the UK, USA, Australia, the Netherlands and South Africa. The literature review thus identified the major governance concerns at auditing firms that contributed to corporate failures. From the literature, it was evident the lack of independent oversight at auditing firms was one of the major contributors.

The key findings of the literature study are outlined below.

Literature findings

i. The UK has experienced major corporate failures, such as Robert Maxwell, Barings Bank, BP, Tesco, Carillion and Patisserie Valerie, to mention only a few. The literature highlighted how unethical behaviour and a lack of independence between the corporations and the auditors contributed to these failures.

ii. In the USA, there were many corporate failures, starting with McKesson & Robbins, the infamous Enron scandal, the WorldCom failure, Lehman Brothers and more recently, AIG and GE. The USA also saw the complete collapse of one of the largest auditing firms, Arthur Andersen. These corporate failures and ultimately, the audit firm failure of Arthur Andersen, underscored the importance of corporate governance.

iii. In Australia, the corporate failures of HIH was one of the worst in Australia and as Arthur Andersen was their auditors, governance issues also came to the fore as a major concern. The lack of independence was a key contributor to the failure. The failure of Harris Scarfe emphasised the importance of ethical behaviour by both the corporate entities and the auditing firms.

iv. In the Netherlands, the most significant corporate failure was that of Royal Ahold. The Netherlands is already applying a two-board structure. The benefit of such a structure were indicated in the literature findings on the Royal Ahold failure. The audit firm, Deloitte, put an end to the fraud, identifying irregularities at an early stage. Thus, Ahold was the one case where the auditors did not contribute to the failure due to a lack of corporate governance.

v. Lastly, in South Africa, the literature identified many recent corporate failures, such as Steinhoff, Tongaat Hulett and VBS Bank. KPMG South Africa came under media scrutiny due to their involvement in some of these corporate failures. Other auditing firms, such as Deloitte and PwC, also came under the media spotlight. Nkonki collapsed due to issues of auditor independence, unethical behaviour and a lack of corporate governance. These South African failures undermined public trust, highlighting that the lack of corporate governance in auditing firms is a serious matter that should be addressed.

vi. Many members of the accounting profession claim that the reputation of the profession has been irreparably damaged by corporate scandals. The negative publicity that accountants have brought upon themselves has jeopardised the reputation of the profession and it is time that the reputation of the profession be restored.

vii. From the literature, it can be seen that ethical behaviour and independence are two major concerns in terms of corporate governance in auditing firms. This finding was used to inform the empirical study, with many of the questions addressing the importance and role of an independent oversight board. This is discussed in the empirical findings below.

The following section discusses how research objective 3 was achieved through the empirical study.

Empirical findings

From the issues identified in the literature review, the most prominent was the lack of values, proper internal controls, independence and ethical leadership in auditing firms. It was therefore essential to analyse the application and disclosure of these principles contained in the UK Audit Firm Governance Code within large and medium-sized auditing firms in South Africa. This was achieved through the empirical study, which found that the disclosure of these principles was lacking. This finding could be attributed to the lack of guidance given to auditing firms on corporate governance. The application at the auditing firms, according to the responses of the CEOs, was better than what the disclosure revealed in the content analysis. As a result, the readers of transparency reports may not obtain correct and relevant information to form an informed opinion about the governance at auditing firms. This is a negative finding for the auditing firms. The CEOs of the large and medium-sized auditing firms were mostly in agreement that the principles and provisions contained in the UK Audit Firm Governance Code should be applied to auditing firms in South Africa. This is elaborated on below, with a detailed explanation of each of these principles.

The disclosure on the leadership principle was found to be inadequate, with auditing firms mostly providing information about their EXCO, but very little about their oversight boards. Only two auditing firms disclosed information about their oversight boards. With regards to the application of these principles, the questionnaires found that the leadership principle was mostly applied within the auditing firms. It was also found that seven of the nine auditing firms were currently applying some of the principles contained in King IV. The CEOs also provided their expert opinions on the disclosure of the leadership principle and provisions in the transparency report. The outcome was that almost all of the firms believed that all the provisions contained in the UK Code should be disclosed by South African firms in their transparency reports. This supports the notion that the UK Code could be used to inform the development of a South African code.

With reference to the values principle, the disclosure was more positive, with auditing firms appearing to have the correct polices in place. The concern was thus whether these values are applied as they should be. In terms of the application of the values principle, the CEOs were all in agreement that the responsibilities of the oversight board, as contained in the UK Code, should be applied in South Africa.

In terms of the INEDs principle, the disclosure was not as desired. The auditing firms had disclosed scant information about oversight boards and their independence. This lack of disclosure goes hand in hand with the lack of guidance provided to auditing firms as well as the difficulty of appointing INEDs due to the constraints imposed by APA in South Africa. The application of the INEDs principle was also not as desired, with only two firms having INEDs on their oversight boards. The CEOs agreed about the responsibilities of the INEDs, but stated that the amount of INEDs on the oversight board should not be determined by a code. With reference to the information that should be disclosed about INEDs, the auditing firms were mostly in agreement, with the majority supporting the disclosure requirements contained in the UK Code. With regards to the characteristics and the rights and responsibilities of INEDs, the CEOs were mostly in agreement that the principles and provisions in the UK Code should be applied in South Africa.

The disclosure of the operations principle was found to be inadequate. Many of the principles and provisions were not disclosed by the majority of the auditing firms. The empirical study found that the EXCO of the auditing firms was not applying the operations principle as stated in the UK Code. The CEOs concurred that the disclosure was not optimal, thus supporting the content analysis findings. The policies and procedures with regards to whistleblowing were mostly implemented in the auditing firms. The CEOs indicated that their application of compliance was good, providing an indication that the auditing firms would easily be able to implement the operations principle and provision contained in the UK Code. However, their disclosure would need to improve, which could be achieved through a formal South African Audit Firm Governance Code.

Conclusion for research objective 3:

The literature revealed that there were numerous corporate failures in the world. In many of the cases, the weak corporate governance at the auditing firms contributed to these failures. This lack of corporate governance could stem from the fact that there is only one corporate governance code for auditing firms in the world—the UK Audit Firm Governance Code. This means that most countries do not have a standardised code or framework which governs auditing firms. There is a need for such codes in many countries and South Africa is no exception. The empirical findings revealed that the principles contained in the UK Audit Firm Governance Code are mostly accepted by the majority of the auditing firms in South Africa as best practice and should be used as the basis for the development of a South African code, or possibly, a sector supplement in future King Code iterations.

7.2.4 Research objective 4: Current legal and governance structures in auditing firms as well as the challenges with implementing corporate governance within auditing firms

This research objective aimed to review the literature on the legal and governance structures of auditing firms. It also discussed the challenges that auditing firms are currently facing with regards to the implementation of governance. The lack of research focusing on auditing firms was evident, affirming the importance of this study.

The key findings in the literature study are outlined below.

Literature findings

i. The literature found that most auditing firms were generally set up as partnerships or personal liability (incorporated) companies.

ii. Most auditing firms elect directors to be members of the EXCO, which is responsible for the day-to-day operations of the firm. The EXCO is not responsible for the governance of the audit firm.

iii. Due to the requirements in the legislation, all shareholders and directors of auditing firms must be auditors registered with the IRBA. This makes it impossible to appoint INEDs to the EXCO. For this reason, there is a need for the internal appointment of an independent oversight board, which would provide independent governance and oversight to the EXCO and the audit firm.

iv. There is currently no specific corporate governance code for auditing firms in South Africa and thus auditing firms have applied very few corporate governance principles. Moreover, not all firms have appointed independent oversight boards or applied a two-tier board structure.

v. The literature also found that there are several codes or pieces of legislation available that regulate auditing firms. However, these contain no detailed guidelines on how South African auditing firms could practice corporate governance. Many of these codes and legislation focus on audit quality and the individual auditor, but not on the audit firm itself and how it should be governed.

The following section discusses how research objective 4 was achieved through the empirical study.

Empirical findings

The content analysis of disclosures in the transparency reports confirmed that auditing firms are either partnerships or personal liability (incorporated) companies. The partnership legal structure is applied far less that the incorporated legal structure. The content analysis also indicated that very few auditing firms disclose information about their oversight boards. All of the auditing firms revealed that they appointed an EXCO, but no INEDs were appointed to these committees.

The empirical questionnaire found that auditing firms are unable to appoint INEDs to their EXCO due to the limitations created by the APA. The UK Audit Firm Governance Code suggests that an independent oversight board should be established to appoint INEDs to auditing firms. The questionnaire found that two of the South African auditing firms had already appointed an oversight board and only one of the auditing firms had at least three INEDs on its oversight board. This is certainly a step in the right direction, with this audit firm leading by example, demonstrating to other South African firms that this is possible.

The CEOs also provided their expert opinions on the challenges that auditing firms face in appointing INEDs and in implementing the principles of a corporate governance code. Most of the challenges were linked to financial constraints and limited resources. Some of the CEOs also pointed out that it was difficult to appoint INEDs within an audit firm structure and to identify individuals who were fully independent. Some of the CEOs also maintained that King IV should be adapted for auditing firms. This confirmed the need for a sector supplement for auditing firms in future King Code iterations.

Conclusion for research objective 4:

This research objective was achieved as the study added to the body of knowledge on auditing firms and their legal and governance structures. All auditing firms have an EXCO, but not all auditing firms have an independent South African oversight board. The literature also emphasised the need for change in the regulation of auditing firms in South Africa. There is also a need for guidance through a code which would guide auditing firms on how to govern their firms and how to appoint INEDs to provide governance oversight. This would create consistency across all auditing firms, ensuring that transparency reports provide relevant governance information. The challenges identified in the literature and empirical findings should be taken into consideration during the development of a South African audit firm governance code.

7.2.5 Research objective 5: Governance disclosure of auditing firms in their transparency reports

This objective sought to determine which of the disclosure principles and provisions contained in the UK Audit Firm Governance Code were currently being disclosed by South African auditing firms in their transparency reports. This would identify the current disclosure as well as the whether the auditing firms were already applying some governance principles and provisions as contained in the UK Audit Firm Governance Code. Should the firms already be disclosing the majority of the principles and provisions, it would be easier for auditing firms to implement a South African governance code in future.

The key findings in the literature study are outlined below.

Literature findings

i. Auditing firms are expected to release any information that might affect market confidence and improve transparency (Kumar & Zattoni, 2014; Mallin, 2002; OECD, 2015b). The literature confirms that issuing a transparency report is important. The IRBA (2018) explains that the release of a transparency report provides the public with information on various aspects of the firm and its operations. This is affirmed by the IAASB (2014), which states that audit firm transparency reports assist third parties, such as the public and users of the audited financial statements, to understand the characteristics of the individual audit firm and the drivers of audit quality in the firm. According to La Rosa et al. (2018), transparency reports provide meaningful information about audit firm quality and independence.

ii. Huddart (2013) maintains that the call for greater transparency and disclosure by auditing firms is supported by the high-profile audit firm failures and the lack of confidence in the financial market in the post-global financial crisis era.

iii. The IRBA suggests that all auditing firms issue a transparency report, however, at this point it is not compulsory for auditing firms to do so.

The following section discusses how research objective 5 was achieved through the empirical study.

Empirical findings

The principles 'reporting and dialogue' in the UK Code assisted in achieving this objective.

The findings of the content analysis revealed that the disclosure of the reporting principle was very poor. However, the questionnaire indicated that the auditing firms were applying this reporting principle to some extent. This finding contradicted those of the content analysis. The CEOs of the auditing firms indicated that they applied the principle and provisions, except for those relating to the audit committee.

The disclosure of the dialogue principle was very poor in the transparency reports. The empirical research found that the CEOs believed that the dialogue principle contained in the UK Code was important and should applied in South African auditing firms. Once again, this is an indication that the CEOs agree that the principles are important, but the lack of guidance on how to apply and disclose them creates a weak governance environment.

Conclusion of research objective 5:

The empirical research found that the disclosure of corporate governance information in the transparency reports and integrated reports was not always of the quality and quantity that would be expected of reputable companies.

The lack of disclosure reduces the reliance that stakeholders can place on the corporate governance of the auditing firms. This has an impact on public trust in the profession. The minimal disclosure by auditing firms confirms that the firms appear unaware of the information that they should be disclosing in their transparency reports. There is a strong need for guidelines on the disclosure that is expected of auditing firms. Formal guidelines or a code would ensure that auditing firms disclose necessary and consistent information to the public.

7.2.6 Research objective 6: Current corporate governance practice at auditing firms and the expert opinions of the CEOs of auditing firms on corporate governance in auditing firms

The aim of this objective was to determine which of the principles and provisions contained in the UK Audit Firm Governance Code were being applied in South African auditing firms. The empirical questionnaire was used to obtain the expert opinions of CEOs on the importance of a corporate governance code for South African auditing firms. This was to help establish whether the auditing firms would accept the development of such code for the South African context. The questionnaire also obtained some expert opinions from the CEOs on the difficulties in implementing such a code in South Africa.

The key findings of the literature review are outlined below.

Literature findings

The following section discusses how research objective 6 was achieved through the literature review.

i. According to Sikka (2003), any reform of auditing and accountancy should bring about a major change in the values that govern auditing firms.

iv. According to the UK's FRC (2010), strong audit firm governance is a way of maintaining public trust.

v. Aberian (2019) observes that the corporate structure of some auditing firms seems to be flawed as they fail to apply codes of corporate governance.

vi. Currently in South Africa, there is no corporate governance structure that regulates the corporate governance of auditing firms. From the literature, it is evident that the UK is at the forefront of corporate governance for auditing firms. No evidence of other corporate governance codes, specifically with reference to auditing firms, could be found.

vii. For this reason, the study sought to determine the current application of corporate governance in South African firms to emphasise the gap in the research and the need to draft a South African Audit Firm Governance Code or include a sector supplement for auditing firms in future King Code iterations.

Empirical findings

The empirical findings illustrate that the role of an audit firm governance code for South African auditing firms is critical for the effective application and disclosure of corporate governance principles in South Africa auditing firms. The key findings from the empirical research are summarised below.

i. With reference to the leadership principle, it was found that seven of the auditing firms had an oversight board but of these, only two disclosed such information. Although there was an evident lack of disclosure on many of the leadership principles and provisions, the majority of the auditing firms stated they applied these principles. Seven of the auditing firms indicated they applied some of the King IV principles. From the CEOs' comments, it seems that the appointment of INEDs was where they fell short. The majority of the CEOs believed that leadership provisions should be disclosed in auditing firms' transparency reports.

ii. With reference to the values principle, the empirical study found that application was good. The CEOs agreed that all the principles and provisions on values should be applied by the oversight board. The CEOs also stressed the importance of an oversight board and its role in an audit firm.

iii. With reference to the principle of INEDs, the empirical study found that its application in the auditing firms was not as desired. These findings emphasised the challenges of auditing firms in appointing INEDs. The majority of the CEOs agreed that the involvement of INEDs was important, but that the number of INEDs on the oversight board should not have to be specified as at least three. The majority of the CEOs concurred with the characteristics of INEDs as well as their responsibilities, as described in the UK Code.

iv. With reference to the operations principle, the application by the EXCOs of South African auditing firms was found to be lacking. The principles dealing with the policies and procedures were applied to some extent. The auditing firms were in agreement that the INEDs of the oversight board should be involved in protecting the public interest.

v. With reference to the empirical findings on the reporting principle, the application in the auditing firms was found to be lacking. The provisions dealing with the audit committee were not applied to the desired extent as only three of the firms had audit committees.

vi. With reference to the dialogue principle, the auditing firms concurred that mutual communication and understanding with shareholders were important, but not all were in agreement that the policies and procedures should be disclosed and that the nature and extent of the involvement of INEDs in the dialogue should be disclosed.

vii. The CEOs believed that an ‘apply and explain’ framework would be the most suitable for a future code of corporate governance for auditing firms.

viii. The CEOs conveyed that there would be some difficulties in implementing an audit firm governance code in South Africa, but these would be mostly linked to resources.

ix. The majority of the CEOs agreed that an oversight board should be appointed within auditing firms.

x. The CEOs indicated that separate frameworks for the audit and non-audit parts of the firms would not be necessary.

xi. The CEOs stated that the key areas of focus should be independence, managing conflicts of interest, ethics, leadership and audit quality.

xii. In the additional commentary provided in the questionnaire, the CEOs indicated that the audit profession should restore public interest and that a corporate governance code for auditing firms in South Africa should be developed.

Conclusion for research objective 6:

From the information obtained, it is evident that corporate governance plays a critical role in the governance structures of auditing firms and that auditing firms also understand its importance. However, auditing firms in South Africa are facing serious challenges, such as finding members who are independent, have the relevant skills, experience and competence and who are prepared to serve on an oversight board of an audit firm. Some of the auditing firms also indicated that limited financial resources would prevent them from implementing strict corporate governance guidelines.

From the findings, it can be concluded that the UK Audit Firm Governance Code would be a good starting point to develop a code for South African auditing firms.

7.3 Recommendations

7.3.1 Best practice recommendations for governance in auditing firms

i. It is recommended that all auditing firms consider the implementation and practice of good corporate governance to enjoy the benefits that it offers. As the principles embodied in King IV are similar to those contained in the UK Audit Firm Governance Code, the auditing firms could start by implementing the relevant principles of King IV until further developments in future.

ii. Corporate governance should not merely exist as a 'tick box' exercise, but should be effective and applied for the benefits that it will offer to auditing firms and all stakeholders. The corporate governance practices and disclosures should be supported by the EXCO and all shareholders of the audit firm.

iii. An oversight board should be appointed by auditing firms and should be supported by the EXCO. The oversight board should have all the necessary resources, support and authority to effectively discharge its duties and responsibilities. The oversight board should consist of members who are independent and who have the necessary financial expertise and knowledge.

iv. The oversight board should diligently perform the responsibilities entrusted to it by the oversight board charter. However, members must be careful not to accept responsibilities that they are not qualified for, have no time to perform or that fall outside their remit.
v. The oversight board should report to the shareholders and other stakeholders of the audit firm.
vi. The oversight board should ensure that sufficient information is provided in the transparency report on the oversight board structure, functioning and responsibilities so provide readers with an informed view of the board.
vii. Auditing firms should consider combining their transparency reports and integrated reports. This would minimise the duplication of the information in these two reports.

7.3.2 Regulatory and statutory recommendations

7.3.2.1 King IV

It is recommended that the IoDSA consider the inclusion of a sector supplement for auditing firms in future King Code iterations.

7.3.2.2 IRBA

The IRBA is responsible for regulating the auditing profession. In the IRBA's 2019/2020 Annual Report, former CEO Bernard Agulhas claims that governments and audit authorities are now calling for changes internationally and are keenly examining recommendations and research on reform of the audit profession and how it is governed. He states that the IRBA is specifically focusing on developments in the UK. The current negative state of the profession brought on by the unprofessional actions of a few has undermined trust in the auditing profession. He stated that the regulator would work even harder to restore confidence and make the profession one of the most trusted and valued once again. The auditing industry was called on to review current practices to restore faith in the profession. Such trust would be strengthened if all participants in the financial reporting chain—including management, those in charge of governance and investors— assumed the obligation to rebuild the requisite trust (IRBA, 2019). This literature from 2019 emphasises that the IRBA is already considering reform, with the aim of improving governance in auditing firms. The IRBA should consider using the findings of this study and the developments in the UK, to provide guidelines for auditing firms on corporate governance.

7.3.2.3 Audit Profession Act (APA)

It is recommended that an amendment of the APA be considered to facilitate the appointment of INEDs for auditing firms.

7.3.2.4 Institutions and professional bodies

Professional bodies and institutions such as SAICA, IoD and SAAPTI should consider providing best practice standards on corporate governance at auditing firms. Similarly, the IoD (or the IRBA, as the regulator) should consider providing a statement for auditing firms, giving them guidance in corporate governance practices (such as the UK Audit Firm Governance Code provided by the FRC).

Consideration should also be given to the establishment of a register of INEDs who are available for selection to oversight boards. To qualify as an accredited member, certain requirements would need to be met, including independence, minimum experience, financial literacy and other governance aspects.

7.3.2.5 Media

Informed and credible journalism can play a significant role in promoting corporate governance in auditing firms and the value it can add for the firm and all stakeholders. In this regard, it is recommended that academics, practitioners and others provide journalists with articles, information and facts that can be published to create greater awareness of the value of corporate governance at auditing firms.

7.4 Areas for future research

i. The application of corporate governance at smaller auditing firms should be investigated. These smaller auditing firms may have unique circumstances that require different corporate governance measures.

ii. The application of corporate governance in auditing firms internationally should be investigated. As the UK is the only country with a corporate governance code for auditing firms, other countries would also need to draft such a code for their auditing firms.
iii. A corporate governance code for South African auditing firms should be developed. The unique circumstances, challenges and opportunities of the auditing profession should be taken into consideration. South Africa is a leader in corporate governance and could play an important role in upliftment in this field.
iv. Amendments to the APA should be considered to ensure that auditing firms in South Africa are able to appoint INEDs.

7.5 Limitations of the study

The results of this study focused on large and medium-sized auditing firms in South Africa, consequently, generalisation is subjective. The scope of this study is limited to the population outlined in Chapter 1 and it is acknowledged that many other aspects could have influenced the research problem.

7.6 Contributions to the existing body of knowledge

This study contributed to the description of corporate governance structures in large and medium-sized auditing firms. These auditing firms all have 20 or more audit partners. The findings of the study provide a holistic view of the corporate governance practices and disclosures, which could be used by professional institutions, such as SAAPTI and the IoDSA, to develop a corporate governance code specifically for auditing firms in South Africa. The results could also be used by auditing firms to add value; by adopting the guidelines suggested in this study, the firms could improve their application and disclosure of corporate governance and provide transparent and valuable information to the public on their governance structures.

This study contributed to the existing body of knowledge in the area of corporate governance in auditing firms by analysing the corporate governance disclosure and practices of large and medium-sized auditing firms in South Africa. This could be used in local and global studies to compare practices and disclosure in other auditing firms in the world.

The study identified six key corporate governance principles from the UK Audit Firm Governance Code, which are similar to many of the principles found in King IV. The challenges facing auditing firms with regard to corporate governance were also identified. The study then discussed the principles that should be considered by auditing firms to improve their corporate governance structures.

Lastly the study contributed to the research design and methodology for auditing studies and could be used as a benchmark for data collection. In this regard, SPSS software was used to quantify the qualitative research data, which assisted in interpreting the results.

Thus, the study contributes to the limited body of knowledge on corporate governance in auditing firms, not only internationally, but more specifically, in South Africa. It is suggested that using the guidelines emerging from this study will assist auditing firms to improve their corporate governance structures.

7.7 Conclusion

This study found that the application of corporate governance in large and medium-sized auditing firms is inadequate. This was evident from the findings of the empirical research, the content analysis and the responses of the CEOs of auditing firms. The main reason for the lack of corporate governance in South African auditing firms is attributed to the fact that there is no South African corporate governance code for auditing firms. Thus, auditing firms are applying elements of King IV as they see fit and wish. Moreover, the APA makes it impossible for auditing firms to appoint INEDs as members of EXCO. For this reason, some auditing firms have appointed oversight boards, but unfortunately, only two of the firms have INEDs on these boards. As stated by Maranga (2018), oversight boards should implement internal controls in auditing firms to ensure good corporate governance. This would foster honesty, openness and accountability in the firms. Corporate governance may be indicated through the EXCO, the oversight board and auditing. Accountants and auditors must protect shareholders' interests, enforce policies to ensure accountability and transparency and perform regular risk assessments (Maranga, 2018).

The primary objective of this study, as stated in Chapter 1, Section 1.8, was to provide guidance to auditing firms on practices and structures that should be implemented to establish oversight on the corporate governance of auditing firms. This guidance was provided in Chapter 7, section 7.3. The findings in Chapter 6 can also be used by auditing firms to implement the principles and provisions of the UK Audit Firm Governance Code. South African audit forms can make use of these guidelines to protect the public interest, to change the negative perceptions currently associated with the audit profession and to provide honest and transparent information to all stakeholders.

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ANNEXURE A: Other corporate governance developments around the world

According to the The European Corporate Governance Institute (ECGI) (2020), the following corporate governance codes also exist around the world.

Country	Detail regarding the corporate governance code
Austria	The Austrian Working Group for Corporate Governance created a set of rules and standards for the responsible management of companies in Austria. The Austrian Corporate Governance Code is principally non-binding and only applies to listed companies.
Belgium	Belgian corporate governance practices for listed companies have been partially codified in the Belgian Company Code.
Brazil	The Brazilian Corporate Governance Code is applicable to listed companies and follows a ‘comply or explain’ approach.
Canada	Corporate governance practices in Canada are shaped by legal rules and best practices promoted by institutional shareholder groups, the media and professional associations such as the Institute of Corporate Directors. Sources of legal rules include provincial corporate statutes, securities laws and rules, stock exchange requirements and common law as well as a wide variety of other regulatory statutes, regulations and policies.
Denmark	The Danish corporate governance regime consists of hard law as well as soft law provisions.
Finland	Finnish corporate governance is based primarily on the Finnish Companies Act. The Act regulates the governance of companies such as the role of the board of directors, managing directors and shareholders as well as their duties and responsibilities.
France	Corporate governance rules are mainly set out in statutory provisions contained in the French Commercial Code and in recommendations contained in corporate governance codes (such as the French Association of Private Enterprises (AFEP), Movement of French Enterprises (MEDEF) Code) or in

	positions expressed by various professional bodies and associations. Indeed, the AFEP-MEDEF Code has become a reference in matters of corporate governance. It is based on recommendations issued over the past 21 years and sets the corporate governance standards for listed companies.
Germany	The corporate governance of German stock corporations (*Aktiengesellschaft*), the legal form most common among listed companies in Germany, is determined by both statutory law and non-binding best practice rules.
Ghana	The corporate governance regime for listed companies in Ghana is essentially a combination of statutory law, subsidiary legislation and regulatory guidelines and directives. The Ghanaian Corporate Governance Code does not have the force of law and is merely used as a benchmark for assessing the governance practices of listed companies and companies that operate within the securities industry.
India	The Indian corporate governance framework is composed of statutes and regulations that require supervision by multiple regulators.
Indonesia	A company's articles of association are the general governance document of the company. In practice, companies normally also prepare their own corporate governance manual as a reference for the companies' ethics and business practices.
Ireland	In Ireland, companies listed on the principal Irish securities market, Euronext Dublin, are required to comply with both the UK Corporate Governance Code (Corporate Governance Code) and the Irish Corporate Governance Annex.
Japan	Companies in Japan are generally regulated by the Companies Act. In addition, Japan's Corporate Governance Code was released on 1 June 2015 and was most recently revised on 1 June 2018. The Code, which is applicable to all companies listed on securities exchanges in Japan, establishes fundamental principles for effective corporate governance.
Kenya	The Kenyan capital market is regulated by the Capital Markets Authority (CMA). In 2016, the CMA published a code for corporate governance practices for publicly listed companies. The Code replaced the Guidelines on Corporate Governance Practices by Public Listed Companies in Kenya, 2002. The code

	was informed by the need to respond to the changing business environment coupled with the desire to align Kenyan local standards to global best practice to promote institutional strengthening for listed companies.
Luxemburg	Luxembourg's main statutes on corporate governance include the Companies Act, the EU Market Abuse Regulation and the Securitisation Act. The Companies Act was reviewed in 2016 to modernise Luxembourg corporate law. A consolidated version of the Act was published in December 2017.
Nigeria	The Nigerian corporate governance regime is characterised by a combination of a statutory framework and subsidiary legislation enacted by the relevant regulatory authorities. These laws can be divided into two categories: general laws and sector-specific laws. While the general laws govern every entity incorporated in Nigeria, the sector-specific laws govern only companies that operate within their specific sector or industry.
Norway	Iimportant guidelines for corporate governance in listed companies have been established in the Norwegian Code of Practice for Corporate Governance (NCCG). The NCCG provides Norwegian listed companies with guidelines for governing the relationship between shareholders, boards of directors and executive management more comprehensively than the applicable legislation. The NCCG consists of 15 recommended principles of corporate governance, each of which is coupled with explanatory commentaries.
Poland	In Poland, general corporate governance rules applicable to companies, including listed companies, are laid down in the Commercial Companies Code of 2000 (CCC), which replaced the former Commercial Code of 1934. The CCC sets out the general duties and powers of the various corporate bodies, as well as rules on representation, conflicts of interest and the liability of management board members.
Portugal	The main legal sources of corporate governance rules in Portugal are the Portuguese Commercial Companies Code, enacted by Decree-Law No. 262/86, of 2 September, which sets out the general legal framework governing companies.

Russia	Best practice provisions for listed companies are set out in the Corporate Governance Code and the listing rules of licensed stock exchanges.
Singapore	The Singapore corporate governance regulatory framework is contained in certain mandatory rules, comprising the Companies Act, the Securities and Futures Act and, for companies listed on the Singapore Exchange, the Listing Manual. Other benchmarks include best practice recommendations as set out in the Code of Corporate Governance and the accompanying Practice Guidance issued by the Monetary Authority of Singapore. The Code was first introduced in Singapore in March 2001 and was revised in 2005, 2012 and 2018. The revised 2018 Code applies with effect to annual reports covering financial years commencing from 1 January 2019.
Sweden	The report contains the Board's activity report and statistics on companies' application of the Swedish Corporate Governance Code.
Switzerland	The statutory corporate law set out in the Swiss Code of Obligations (CO) is the main source of Swiss corporate governance regulation. The CO applies to private and public companies.

ANNEXURE B: Principles of the UK combined code

According to the Financial Reporting Council (2019), the 2018 UK Combined Code consists of the following corporate governance principles.

1. Board leadership and company purpose.	a) A successful company is led by an effective and entrepreneurial board, whose role is to promote the long-term sustainable success of the company, generating value for shareholders and contributing to wider society. b) The board should establish the company's purpose, values and strategy and satisfy itself that these and its culture are aligned. All directors must act with integrity, lead by example and promote the desired culture. c) The board should ensure that the necessary resources are in place for the company to meet its objectives and measure performance against them. The board should also establish a framework of prudent and effective controls, which enable risk to be assessed and managed. d) In order for the company to meet its responsibilities to shareholders and stakeholders, the board should ensure effective engagement with and encourage participation from, these parties. e) The board should ensure that workforce policies and practices are consistent with the company's values and support its long-term sustainable success. The workforce should be able to raise any matters of concern.
2. Division of responsibilities:	(f) The chair leads the board and is responsible for its overall effectiveness in directing the company. The chair should demonstrate objective judgment throughout their tenure and promote a culture of openness and debate. In addition, the chair facilitates constructive board relations and the effective contribution of all non-executive directors and ensures that directors receive accurate, timely and clear information.

	(g) The board should include an appropriate combination of executive and non-executive directors (and in particular, independent non-executive directors), so that no one individual or small group of individuals can dominate the board's decision-making. There should be a clear division of responsibilities between the leadership of the board and the executive leadership of the company's business. This is supported by Dedman (2016), who states that according to the agency view of the Combined Code, [a] chief executive should not go on to be chairman of the same company because this empowers boards against powerful CEOs who are reluctant to step aside for a successor. Further, a chairman who is independent upon appointment, is believed to provide effective board oversight and monitoring of the incoming CEO. (h) Non-executive directors should have sufficient time to meet their board responsibilities. They should provide constructive challenge, strategic guidance and specialist advice as well as holding management to account. (i) The board, supported by the company secretary, should ensure that it has the policies, processes, information, time and resources it needs to function effectively and efficiently.
3. Composition, succession and evaluation:	j) Appointments to the board should be subject to a formal, rigorous and transparent procedure and an effective succession plan should be maintained for board and senior management. Both appointments and succession plans should be based on merit and objective criteria and, within this context, should promote diversity of gender, social and ethnic backgrounds, cognitive and personal strengths. k) The board and its committees should have a combination of skills, experience and knowledge. Consideration should be given to the length of service of the board as a whole and membership should be regularly refreshed.

	l) Annual evaluation of the board should consider its composition, diversity and how effectively members work together to achieve objectives. Individual evaluation should demonstrate whether each director continues to contribute effectively.
4. Audit, risk and internal control:	(m) The board should establish formal and transparent policies and procedures to ensure the independence and effectiveness of internal and external audit functions and satisfy itself on the integrity of financial and narrative statements. (n) The board should present a fair, balanced and understandable assessment of the company's position and prospects. (o) The board should establish procedures to manage risk, oversee the internal control framework and determine the nature and extent of the principal risks the company is willing to take on to achieve its long-term strategic objectives.
5. Remuneration:	p) Remuneration policies and practices should be designed to support strategy and promote long-term sustainable success. Executive remuneration should be aligned to company purpose and values and be clearly linked to the successful delivery of the company's long-term strategy. q) A formal and transparent procedure for developing policy on executive remuneration and determining director and senior management remuneration should be established. No director should be involved in deciding their own remuneration outcome. r) Directors should exercise independent judgment and discretion when authorising remuneration outcomes, taking account of company and individual performance and wider circumstances.

ANNEXURE C: Audit firm corporate governance code by the FRC

This annexure provides the principles of the Audit Firm Governance Code, as published by the FRC (2016).

Leadership	• **Owner accountability principle.** The management of a firm should be accountable to the firm's owners and no individual should have unfettered powers of decision. • **Management principle:** A firm should have effective management which has responsibility and clear authority for running the firm (Financial Reporting Council, 2016).
Values	• **Professionalism principle:** A firm should perform quality work by exercising judgment and upholding values of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour in a way that properly takes the public interest into consideration and meets auditing and ethical standards. • **Governance principle:** A firm should publicly commit itself to this Audit Firm Governance Code. • **Openness principle:** A firm should maintain a culture of openness which encourages people to consult and share problems, knowledge and experience in order to achieve quality work in a way that properly takes the public interest into consideration (Financial Reporting Council, 2016).
Independent Non-Executives (INEDs)	• **Involvement of INE principle:** A firm should appoint INEDs to the governance structure who, through their involvement, collectively enhance the firm's performance in meeting the purpose of the Audit Firm Governance Code. • **Characteristics of INE principle:** The INEDs' duty of care is to the firm. They should command the respect of the firm's owners and collectively enhance shareholder confidence by virtue of their

	independence, number, stature, experience and expertise. They should have a balance of relevant skills and experience including audit and a regulated sector. At least one INED should have competence in accounting and/or auditing, gained, for example, from a role in an audit firm. • **Rights and responsibilities of INE principle:** INEDs of a firm should have rights consistent with their role including the right of access to relevant information and people to the extent permitted by law or regulation, the right to report a fundamental disagreement regarding the firm to its owners and, where ultimately this cannot be resolved and the INED resigns, to report this resignation publicly (Financial Reporting Council, 2016).
Operations	• **Compliance principle:** A firm should comply with professional standards and applicable legal and regulatory requirements. Operations should be conducted in a way that promotes audit quality and the reputation of the firm. The INEDs should be involved in the oversight of operations. • **Risk management principle:** A firm should maintain a sound system of internal control and risk management over the operations of the firm as a whole to safeguard the firm and reassure stakeholders. • **People management principle:** A firm should apply policies and procedures for managing people across the whole firm, supporting commitment to professionalism, openness and risk management principles of the Audit Firm Governance Code. • **Whistleblowing principle:** A firm should establish and apply confidential whistleblowing policies and procedures across the firm which enable people to report, without fear, any concerns about the firm's commitment to quality work and professional judgment and values in a way that properly takes the public interest into consideration. The INEDs should be satisfied that there is an effective whistleblowing process in place (Financial Reporting Council, 2016).

Reporting	• **Internal reporting principle:** The management of a firm should ensure that members of its governance structures, including owners and INEDs, are supplied with information in a timely manner and in a form and of a quality appropriate to enable them to discharge their duties. • **Governance reporting principle:** A firm should publicly report how it has applied in practice each of the principles of the Audit Firm Governance Code and make a statement on its compliance with the Code's provisions or give a considered explanation for any non-compliance. • **Transparency principle:** A firm should publish on an annual basis in its transparency report a commentary on the firm's performance, position and prospects. • **Reporting quality principle:** A firm should establish formal and transparent arrangements for monitoring the quality of external reporting and for maintaining an appropriate relationship with the firm's auditors. • **Financial statements principle:** A firm should publish audited financial statements prepared in accordance with a recognised financial reporting framework such as International Financial Reporting Standards or UK GAAP. Moreover, these statements, should be clear and concise (Financial Reporting Council, 2016).
Dialogue	• **Firm dialogue principle:** A firm should have dialogue with listed company shareholders as well as with listed companies and their audit committees, about matters covered by the Audit Firm Governance Code. This is intended to enhance mutual communication and understanding and ensure that the firm keeps in touch with shareholder opinion, issues and concerns. • **Shareholder dialogue principle:** Shareholders should have dialogue with auditing firms to enhance mutual communication and understanding.

	• **Informed voting principle:** Shareholders should have dialogue with listed companies on the process of recommending the appointment and re-appointment of auditors and should make considered use of votes in relation to such recommendations (Financial Reporting Council, 2016).

ANNEXURE D: Comparison of the UK corporate governance code and auditing firms

Below is a comparison between the UK Corporate Governance Code and how this code could be applied to auditing firms (potentially already incorporated into the UK Audit Firm Code) (Financial Reporting Council, 2016).

UK Corporate Governance Code	**Potentially relevant to auditing firms?**
Role of the Board Every company should be headed by an effective board which is collectively responsible for the long-term success of the company.	Already in
A1.1 The board should meet sufficiently regularly to discharge its duties effectively. There should be a formal schedule of matters specifically reserved for its decision. The annual report should include a statement of how the board operates, including a high-level statement of which types of decisions are to be taken by the board and which are to be delegated to management.	✔
A.1.2 The annual report should identify the chairman, the deputy chairman (where there is one), the chief executive, the senior independent director and the chairmen and members of the board committees. It should also set out the number of meetings of the board and those committees and individual attendance by directors.	Already in

A.1.3 The company should arrange appropriate insurance cover in respect of legal action against its directors.	Already in (in the context of INEDs)
Division of responsibilities There should be a clear division of responsibilities at the head of the company between the running of the board and the executive responsibility for the running of the company's business. No one individual should have unfettered powers of decision.	✔
A.2.1 The roles of chairman and chief executive should not be exercised by the same individual. The division of responsibilities between the chairman and chief executive should be clearly established, set out in writing and agreed on by the board.	✔
The chairman The chairman is responsible for leadership of the board and ensuring its effectiveness in all aspects of its role.	✔
A.3.1 The chairman should, upon appointment, meet the independence criteria set out in B.1.1 below. A chief executive should not go on to be chairman of the same company. If exceptionally a board decides that a chief executive should become chairman, the board should consult major shareholders in advance and should set out its reasons to shareholders at the time of the appointment and in the next annual report.	✔
Non-executive directors	✔

As part of their role as members of a unitary board, non-executive directors should constructively challenge and help develop proposals on strategy.	In the context of INEDs
A.4.1 The board should appoint one of the INEDs to be the senior independent director to act as a sounding board for the chairman and to serve as an intermediary for the other directors. The senior independent director should be available to shareholders should they have concerns that have not been resolved through the normal channels, namely, through the chairman, chief executive or other executive directors, or in cases where these channels are inappropriate.	✔ In the context of INEDs
A.4.2 The chairman should hold meetings with the non-executive directors without the executives present. Led by the senior independent director, the non-executive directors should meet without the chairman present at least annually to appraise the chairman's performance and on other occasions, as appropriate.	✔ In the context of INEDs
A.4.3 Where directors have concerns which cannot be resolved about the running of the company or a proposed action, they should ensure that their concerns are recorded in the board minutes. On resignation, a non-executive director should provide a written statement to the chairman for circulation to the board, if they have any such concerns.	Already in (in the context of INEDs)
Composition of the board The board and its committees should have the appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively.	Already in (in the context of INEDs)
B.1.1 The board should identify in the annual report each non-executive director it considers to be independent. The board should determine whether the director is	Already in (in the

independent in character and judgment and whether there are relationships or circumstances which are likely to affect, or could appear to affect, the director's judgment. The board should state its reasons if it determines that a director is independent notwithstanding the existence of relationships or circumstances which may appear relevant to its determination. These include if the director: has been an employee of the company or group within the last five years; has, or has had within the last three years, a material business relationship with the company either directly, or as a partner, shareholder, director or senior employee of a body that has such a relationship with the company; has received or receives additional remuneration from the company apart from a director's fee, participates in the company's share option or a performance related pay scheme, or is a member of the company's pension scheme; has close family ties with any of the company's advisors, directors or senior employees; holds cross-directorships or has significant links with other directors through involvement in other companies or bodies; represents a significant shareholder; or has served on the board for more than nine years from the date of their first election.	context of INEDs)
B.1.3 Except for smaller companies, at least half the board, excluding the chairman, should comprise non-executive directors determined by the board to be independent. A smaller company should have at least two INE directors.	✔ In the context of INEDs
Appointments to the board	✔

There should be a formal, rigorous and transparent procedure for the appointment of new directors to the board	In the context of INEDs
B.2.1. There should be a nomination committee which should lead the process for board appointments and make recommendations to the board. A majority of members of the nomination committee should be INE directors. The chairman or an INE director should chair the committee, but the chairman should not chair the nomination committee when it is dealing with the appointment of a successor to the chairmanship. The nomination committee should make available its terms of reference, explaining its role and the authority delegated to it by the board.	✔ In the context of INEDs
B.2.2 The nomination committee should evaluate the balance of skills, experience, independence and knowledge on the board and, in the light of this evaluation, prepare a description of the role and capabilities required for a particular appointment.	✔ In the context of INEDs
B.2.3 Non-executive directors should be appointed for specified terms subject to re-election and to statutory provisions relating to the removal of a director. Any term beyond six years for a non-executive director should be subject to particularly rigorous review and should take into account the need for progressive refreshing of the board.	✔ In the context of INEDs
B.2.4 A separate section of the annual report should describe the work of the nomination committee, including the process it has used in relation to board appointments. This section should include a description of the board's policy on diversity, including gender, any measurable objectives that it has set for implementing the policy and progress on achieving the objectives. An explanation should be given if neither an external search consultancy nor open advertising has been used in the appointment of a chairman or a non-executive director. Where an	✔ In the context of INEDs

external search consultancy has been used, it should be identified in the annual report and a statement made as to whether it has any other connection with the company.	
Commitment All directors should be able to allocate sufficient time to the company to discharge their responsibilities effectively.	✔
B.3.1 For the appointment of a chairman, the nomination committee should prepare a job specification, including an assessment of the time commitment expected, recognising the need for availability in the event of crises. A chairman's other significant commitments should be disclosed to the board before appointment and included in the annual report. Changes to such commitments should be reported to the board as they arise and their impact explained in the next annual report.	✔
B.3.2 The terms and conditions of appointment of non-executive directors should be made available for inspection. The letter of appointment should set out the expected time commitment. Non-executive directors should undertake that they will have sufficient time to meet what is expected of them. Their other significant commitments should be disclosed to the board before appointment, with a broad indication of the time involved and the board should be informed of subsequent changes.	Already in (in the context of INEDs)
B.3.3 The board should not agree to a full-time executive director taking on more than one non-executive directorship in a Financial Times Stock Exchange (FTSE) 100 company nor the chairmanship of such a company.	✕
Development	✔

All directors should receive induction on joining the board and should regularly update and refresh their skills and knowledge.	
B.4.1 The chairman should ensure that new directors receive a full, formal and tailored induction upon joining the board. As part of this, directors should avail themselves of opportunities to meet major shareholders.	✔
B.4.2 The chairman should regularly review and agree with each director on their training and development needs.	✔
Information and support The board should be supplied in a timely manner with information in a form and of a quality appropriate to enable it to discharge its duties.	Already in (in the context of INEDs)
B.5.1 The board should ensure that directors, especially non-executive directors, have access to independent professional advice at the company's expense where they judge it necessary to discharge their responsibilities as directors. Committees should be provided with sufficient resources to undertake their duties.	Already in (in the context of INEDs)
B.5.2 All directors should have access to the advice and services of the company secretary, who is responsible to the board for ensuring that board procedures are complied with. Both the appointment and removal of the company secretary should be a matter for the board as a whole.	✔
Evaluation The board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors.	Already in

B.6.1 The board should state in the annual report how performance evaluation of the board, its committees and its individual directors has been conducted.	Already in
B.6.2 Evaluation of the board of FTSE 350 companies should be externally facilitated at least every three years. The external facilitator should be identified in the annual report and a statement made as to whether they have any other connection with the company.	Potentially, although FTSE 350 reference would not apply
B.6.3 The non-executive directors, led by the senior independent director, should be responsible for performance evaluation of the chairman, taking into account the views of executive directors.	Potentially
Re-election All directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance.	Already in
B.7.1 All directors of FTSE 350 companies should be subject to annual election by shareholders. All other directors should be subject to election by shareholders at the first annual general meeting after their appointment and to re-election thereafter at intervals of no more than three years. Non-executive directors who have served longer than nine years should be subject to annual re-election. The names of directors submitted for election or re-election should be accompanied by sufficient biographical details and any other relevant information to enable shareholders to take an informed decision on their election.	✕
B.7.2 The board should set out to shareholders in the papers accompanying a resolution to elect a non-executive director why they believe an individual should	✕

be elected. The chairman should confirm to shareholders when proposing re-election that, following formal performance evaluation, the individual's performance continues to be effective and demonstrates commitment to the role.	
Financial and business reporting The board should present a fair, balanced and understandable assessment of the company's position and prospects.	Already in
C.1.1 The directors should explain in the annual report their responsibility for preparing the annual report and accounts and state that they consider the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy. There should be a statement by the auditor about their reporting responsibilities.	Already in
C.1.2 The directors should include in the annual report an explanation of the basis on which the company generates or preserves value over the longer term (the business model) and the strategy for delivering the objectives of the company.	✔
C.1.3 In annual and half-yearly financial statements, the directors should state whether they considered it appropriate to adopt the going concern basis of accounting in preparing them and identify any material uncertainties to the company's ability to continue to do so over a period of at least 12 months from the date of approval of the financial statements.	Already in
Risk management and internal control	Already in

The board is responsible for determining the nature and extent of the principal risks it is willing to take in achieving its strategic objectives. The board should maintain sound risk management and internal control systems.	
C.2.1 The directors should confirm in the annual report that they have carried out a robust assessment of the principal risks facing the company, including those that would threaten its business model, future performance, solvency or liquidity. The directors should describe those risks and explain how they are being managed or mitigated.	Already in
C.2.2 Taking account of the company's current position and principal risks, the directors should explain in the annual report how they have assessed the prospects of the company, over what period they have done so and why they consider that period to be appropriate. The directors should state whether they have a reasonable expectation that the company will be able to continue in operation and meet its liabilities as they fall due over the period of their assessment, drawing attention to any qualifications or assumptions as necessary.	Already in
C.2.3 The board should monitor the company's risk management and internal control systems and, at least annually, carry out a review of their effectiveness and report on that review in the annual report. The monitoring and review should cover all material controls, including financial, operational and compliance controls.	Already in
Audit committee and auditors The board should establish formal and transparent arrangements for considering how they should apply the corporate reporting and risk management and internal control principles and for maintaining an appropriate relationship with the company's auditors.	Already in

C.3.1 The board should establish an audit committee of at least three, or in the case of smaller companies two, INE directors. In smaller companies the company chair may be a member of, but not chair, the committee in addition to the INE directors, provided he or she was considered independent on appointment as chair. The board should satisfy itself that at least one member of the audit committee has recent and relevant financial experience.	Audit Committee requirement already in, although requirements on non-executive participation are not and are potentially relevant.
C.3.2 The main role and responsibilities of the audit committee should be set out in written terms of reference and should include: to monitor the integrity of the financial statements of the company and any formal announcements relating to the company's financial performance, reviewing significant financial reporting judgments contained in them; to review the company's internal financial controls and, unless expressly addressed by a separate board risk committee composed of independent directors, or by the board itself, to review the company's internal control and risk management systems; to monitor and review the effectiveness of the company's internal audit function; to make recommendations to the board, for it to put to the shareholders for their approval in general meeting, in relation to the appointment, re-appointment and	Already in (to some extent)

removal of the external auditor and to approve the remuneration and terms of engagement of the external auditor; to review and monitor the external auditor's independence and objectivity and the effectiveness of the audit process, taking into consideration relevant UK professional and regulatory requirements; to develop and implement policy on the engagement of the external auditor to supply non-audit services, taking into account relevant ethical guidance regarding the provision of non-audit services by the external audit firm; and to report to the board, identifying any matters that may need action or improvement and make recommendations as to the steps to be taken; and to report to the board on how it has discharged its responsibilities.	
C.3.3 The terms of reference of the audit committee, including its role and the authority delegated to it by the board, should be made available.	Already in
C.3.4 Where requested by the board, the audit committee should provide advice on whether the annual report and accounts, taken as a whole, are fair, balanced and understandable and provide the information necessary for shareholders to assess the company's position and performance, business model and strategy.	✔
C.3.5 The audit committee should review arrangements by which company staff may, in confidence, raise concerns about possible improprieties in financial reporting or other matters. The audit committee's objective should be to ensure that arrangements are in place for the proportionate and independent investigation of such matters and for appropriate follow-up action.	Already in (in the context of INEDs)
C.3.6 The audit committee should monitor and review the effectiveness of internal audit activities. Where there is no internal audit function, the audit committee	✔

should consider annually whether there is a need for an internal audit function and make a recommendation to the board and the reasons for the absence of such a function should be explained in the relevant section of the annual report.	
C.3.7 The audit committee should have primary responsibility for making a recommendation on the appointment, reappointment and removal of the external auditors. FTSE 350 companies should put the external audit contract out to tender at least every ten years. If the board does not accept the audit committee's recommendation, it should include in the annual report and in any papers recommending appointment or re-appointment, a statement from the audit committee explaining the recommendation and should set out reasons why the board has taken a different position.	✔
C.3.8 A separate section of the annual report should describe the work of the committee in discharging its responsibilities. The report should include: the significant issues that the committee considered in relation to the financial statements and how these issues were addressed; an explanation of how it has assessed the effectiveness of the external audit process and the approach taken to the appointment or reappointment of the external auditor and information on the length of tenure of the current audit firm and when a tender was last conducted; and if the external auditor provides non-audit services, an explanation of how auditor objectivity and independence are safeguarded.	Already in
Level and components of remuneration	✕

Executive directors' remuneration should promote the long-term success of the company. Performance-related elements should be transparent, stretching and rigorously applied.	
D.1.1 In designing schemes of performance-related remuneration for executive directors, the remuneration committee should follow the provisions in Schedule A to this Code. Schemes should include provisions that would enable the company to recover sums paid or withhold the payment of any sum and specify the circumstances in which it would be appropriate to do so.	✕
D.1.2 Where a company releases an executive director to serve as a non-executive director elsewhere, the remuneration report should include a statement as to whether or not the director will retain such earnings and, if so, what the remuneration will be.	✕
D.1.3 Levels of remuneration for non-executive directors should reflect the time commitment and responsibilities of the role. Remuneration for non-executive directors should not include share options or other performance- related elements. If, exceptionally, options are granted, shareholder approval should be sought in advance and any shares acquired by exercise of the options should be held until at least one year after the non-executive director leaves the board. Holding of share options could be relevant to determining a non-executive director's independence (as set out in provision B.1.1).	✕
D.1.4 The remuneration committee should carefully consider what compensation commitments (including pension contributions and all other elements) their directors' terms of appointment would entail in the event of early termination. The aim should be to avoid rewarding poor performance. The committee should take a	✕

robust line on reducing compensation to reflect departing directors' obligations to mitigate loss.	
D.1.5 Notice or contract periods should be set at one year or less. If it is necessary to offer longer notice or contract periods to new directors recruited from outside, such periods should be reduced to one year or less after the initial period.	✕
Procedure There should be a formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors. No director should be involved in deciding his or her own remuneration.	✕
D.2.1 The board should establish a remuneration committee of at least three, or in the case of smaller companies two, INE directors. In addition, the company chairman may also be a member of, but not chair, the committee if he or she was considered independent on appointment as chairman. The remuneration committee should make available its terms of reference, explaining its role and the authority delegated to it by the board. Where remuneration consultants are appointed, they should be identified in the annual report and a statement made as to whether they have any other connection with the company.	✕
D.2.2 The remuneration committee should have delegated responsibility for setting remuneration for all executive directors and the chairman, including pension rights and any compensation payments. The committee should also recommend and monitor the level and structure of remuneration for senior management. The definition of 'senior management' for this purpose should be determined by the board but should normally include the first layer of management below board level.	✕

D.2.3 The board itself or, where required by the Articles of Association, the shareholders should determine the remuneration of the non-executive directors within the limits set in the Articles of Association. Where permitted by the Articles, the board may, however, delegate this responsibility to a committee, which could include the chief executive.	✕
D.2.4 Shareholders should be invited specifically to approve all new long-term incentive schemes (as defined in the Listing Rules) and significant changes to existing schemes, save in the circumstances permitted by the Listing Rules.	✕
Dialogue with shareholders There should be a dialogue with shareholders based on the mutual understanding of objectives. The board as a whole has responsibility for ensuring that a satisfactory dialogue with shareholders takes place.	✕
E.1.1 The chairman should ensure that the views of shareholders are communicated to the board as a whole. The chairman should discuss governance and strategy with major shareholders. Non-executive directors should be offered the opportunity to attend scheduled meetings with major shareholders and should expect to attend meetings if requested by major shareholders. The senior independent director should attend sufficient meetings with a range of major shareholders to listen to their views in order to help develop a balanced understanding of the issues and concerns of major shareholders.	✕
E.1.2 The board should state in the annual report the steps they have taken to ensure that the members of the board and in particular the non-executive directors, develop an understanding of the views of major shareholders about the company,	✕

for example through direct face-to-face contact, analysts' or brokers' briefings and surveys of shareholder opinion.	
Constructive use of general meetings The board should use general meetings to communicate with investors and to encourage their participation.	✕
E.2.1 At any general meeting, the company should propose a separate resolution on each substantially separate issue and should in particular propose a resolution at the AGM relating to the report and accounts. For each resolution, proxy appointment forms should provide shareholders with the option to direct their proxy to vote either for or against the resolution or to withhold their vote. The proxy form and any announcement of the results of a vote should make it clear that a 'vote withheld' is not a vote in law and will not be counted in the calculation of the proportion of the votes for and against the resolution.	✕
E.2.2 The company should ensure that all valid proxy appointments received for general meetings are properly recorded and counted. For each resolution, where a vote has been taken on a show of hands, the company should ensure that the following information is given at the meeting and made available as soon as reasonably practicable on a website which is maintained by or on behalf of the company: the number of shares in respect of which proxy appointments have been validly made; the number of votes for the resolution; the number of votes against the resolution; and the number of shares in respect of which the vote was directed to be withheld.	✕

When, in the opinion of the board, a significant proportion of votes has been cast against a resolution at any general meeting, the company should explain when announcing the results of voting what actions it intends to take to understand the reasons behind the vote result.	
E2.3 The chairman should arrange for the chairmen of the audit, remuneration and nomination committees to be available to answer questions at the AGM and for all directors to attend.	✕
E.2.4 The company should arrange for the Notice of the AGM and related papers to be sent to shareholders at least 20 working days before the meeting. For other general meetings this should be at least 14 working days in advance.	✕

Financial Reporting Council (2016)

ANNEXURE E: Titles of the USA Sarbanes-Oxley Act

Below is a description of the 11 titles in the Sarbanes-Oxley Act (Murdock & Murdock, 2018).

I.	**Public Company Accounting Oversight Board (PCAOB)**	Title I consists of nine sections and establishes the PCAOB to provide independent oversight of public accounting firms providing audit services ("auditors"). It also creates a central oversight board tasked with registering auditors, defining the specific processes and procedures for compliance audits, inspecting and policing conduct and quality control and enforcing compliance with the specific mandates of SOX (Murdock & Murdock, 2018).
II.	**Auditor Independence**	Title II consists of nine sections and establishes standards for external auditor independence, to limit conflicts of interest. It also addresses new auditor approval requirements, audit partner rotation and auditor reporting requirements. It restricts auditing companies from providing non-audit services (e.g., consulting) for the same clients (Murdock & Murdock, 2018).
III.	**Corporate Responsibility**	Title III consists of eight sections and mandates that senior executives take **individual responsibility** for the accuracy and completeness of corporate financial reports. It defines the interaction of external auditors and corporate audit committees and specifies the responsibility of corporate officers for the accuracy and validity of corporate financial reports. It enumerates specific limits on the behaviours of corporate officers and describes specific forfeitures of benefits and civil penalties for non-compliance. For example, Section 302 requires that the company's 'principal officers' – typically the Chief Executive Officer and Chief Financial Officer – certify and approve the integrity of their company financial reports quarterly (Murdock & Murdock, 2018).

IV.	**Enhanced Financial Disclosures**	Title IV consists of nine sections. It describes enhanced reporting requirements for financial transactions, including off-balance-sheet transactions, pro-forma figures and stock transactions of corporate officers. It requires internal controls for assuring the accuracy of financial reports and disclosures and mandates both audits and reports on those controls. It also requires timely reporting of material changes in financial condition and specific enhanced reviews by the SEC or its agents of corporate reports (Murdock & Murdock, 2018).
V.	**Analyst Conflicts of Interest**	Title V consists of only one section, which includes measures designed to help restore investor confidence in the reporting of securities analysts. It defines the codes of conduct for securities analysts and requires disclosure of knowable conflicts of interest (Murdock & Murdock, 2018).
VI.	**Commission Resources and Authority**	Title VI consists of four sections and defines practices to restore investor confidence in securities analysts. It also defines the SEC's authority to censure or bar securities professionals from practice and defines conditions under which a person can be barred from practising as a broker, advisor or dealer (Murdock & Murdock, 2018).
VII.	**Studies and Reports**	Title VII consists of five sections and requires the Comptroller General and the SEC to perform various studies and report their findings. Studies and reports include the effects of consolidation of public accounting firms, the role of credit rating agencies in the operation of securities markets, securities violations and enforcement actions and whether investment banks assisted Enron, Global Crossing and others to manipulate earnings and obfuscate true financial conditions (Murdock & Murdock, 2018).
VIII.	**Corporate and Criminal Fraud Accountability**	Title VIII consists of seven sections and is also referred to as the *"Corporate and Criminal Fraud Accountability Act of 2002*". It describes specific criminal penalties for manipulation, destruction or alteration of financial records or other interference with

		investigations, while providing certain protections for whistle-blowers (Murdock & Murdock, 2018).
IX.	**White Collar Crime Penalty Enhancement**	Title IX consists of six sections and is also called the White Collar Crime Penalty Enhancement Act of 2002. This section increases the criminal penalties associated with white-collar crime and conspiracies. It recommends stronger sentencing guidelines and specifically adds failure to certify corporate financial reports as a criminal offence (Murdock & Murdock, 2018).
X.	**Corporate Tax Returns**	Title X consists of one section. Section 1001 states that the Chief Executive Officer should sign the company tax return (Murdock & Murdock, 2018).
XI.	**Corporate Fraud Accountability**	Title XI consists of seven sections. Section 1101 recommends a name for this title: *Corporate Fraud Accountability Act of 2002*. It identifies corporate fraud and records tampering as criminal offences and joins those offences to specific penalties. It also revises sentencing guidelines and strengthens their penalties. This enables the SEC to resort to temporarily freezing transactions or payments that have been deemed 'large' or 'unusual' (Murdock & Murdock, 2018).

ANNEXURE F: ASX corporate governance principles and recommendations

1. Lay solid foundations for management and oversight:	A listed entity should clearly delineate the respective roles and responsibilities of its board and management and regularly review their performance.
2. Structure the board to be effective and add value	The board of a listed entity should be of an appropriate size and collectively have the skills, commitment and knowledge of the entity and the industry in which it operates to enable it to discharge its duties effectively and to add value.
3. Instill a culture of acting lawfully, ethically and responsibly	A listed entity should instill and continually reinforce a culture across the organisation of acting lawfully, ethically and responsibly.
4. Safeguard the integrity of corporate reports	A listed entity should have appropriate processes to verify the integrity of its corporate reports.
5. Make timely and balanced disclosure	A listed entity should make timely and balanced disclosure of all matters concerning it that a reasonable person would expect to have a material effect on the price or value of its securities.
6. Respect the rights of security holders	A listed entity should provide its security holders with appropriate information and facilities to allow them to exercise their rights as security holders effectively
7. Recognise and manage risk	A listed entity should establish a sound risk management framework and periodically review the effectiveness of that framework.
8. Remunerate fairly and responsibly	A listed entity should pay director remuneration sufficient to attract and retain high quality directors and design its executive remuneration to attract, retain and motivate high quality senior executives and to align their interests with the creation of value for security holders and with the entity's

	values and risk appetite (ASX Corporate Governance Council, 2019).

ANNEXURE G: Dutch corporate governance code principles

According to the Corporate Governance Code Monitoring Committee (2016), the principles of the 2016 Code are divided into five chapters, with each chapter containing several principles, as stated below.

Chapter 1: Long-term Value Creation	
Principle 1.1 **Long-term value creation**	The management board is responsible for the continuity of the company and its affiliated enterprise.
Principle 1.2 **Risk management**	The company should have adequate internal risk management and control systems in place. The management board is responsible for identifying and managing the risks associated with the company's strategy and activities.
Principle 1.3 **Internal audit function**	The duty of the internal audit function is to assess the design and the operation of the internal risk management and control systems. The management board is responsible for the internal audit function. The supervisory board oversees the internal audit function and maintains regular contact with the person fulfilling this function
Principle 1.4 **Risk management accountability**	The management board should render account of the effectiveness of the design and the operation of the internal risk management and control systems.
Principle 1.5 **Role of the supervisory board**	The supervisory board should supervise the policies carried out by the management board and the general affairs of the company and its affiliated enterprise. In so doing, the supervisory board should also focus on the effectiveness of the company's internal risk management and control systems and the integrity and quality of the financial reporting.

Principle 1.6 **Appointment and assessment of the functioning of the external auditor**	The supervisory board should submit the nomination for the appointment of the external auditor to the general meeting and should supervise the external auditor's functioning.
Principle 1.7 **Performance of the external auditor's work**	The audit committee and the external auditor should discuss the audit plan and the findings of the external auditor based on the work the external auditor has undertaken. The management board and the supervisory board should maintain regular contact with the external auditor.

Chapter 2: Effective Management and Supervision	
Principle 2.1 **Composition and size**	The management board and the supervisory board should be composed so that the requisite expertise, background, competencies and – as regards the supervisory board – independence, are present for them to carry out their duties properly. The size of these two bodies should reflect these requirements.
Principle 2.2 **Appointment, succession and evaluation**	The supervisory board should ensure that a formal and transparent procedure is in place for the appointment and reappointment of management board and supervisory board members as well as a sound plan for the succession of management board and supervisory board members, with due regard to the diversity policy. The functioning of the management board and the supervisory board as a collective and the functioning of individual members should be evaluated on a regular basis.
Principle 2.3 **Organisation of the supervisory board and reports**	The supervisory board should ensure that it functions effectively. It should establish committees to prepare the supervisory board's decision-making. The foregoing does not affect the responsibility of the supervisory board as an organ

	and of the individual members of the supervisory board for obtaining information and forming an independent opinion.
Principle 2.4 Decision-making and functioning	The management board and the supervisory board should ensure that decisions are made in a balanced and effective manner while taking account of the interests of stakeholders. The management board should ensure that information is provided in a timely and sound manner. The management board and the supervisory board should keep their knowledge and skills up to date and spend sufficient time on their duties and responsibilities. They should ensure that, in performing their duties, they have the information that is required for effective decision-making.
Principle 2.5 Culture	The management board is responsible for creating a culture aimed at long-term value creation for the company and its affiliated enterprise. The supervisory board should oversee the activities of the management board in this regard.
Principle 2.6 Misconduct and irregularities	The management board and the supervisory board should be alert to indications of actual or suspected misconduct or irregularities. The management board should establish a procedure for reporting actual misconduct or suspicion of any misconduct or irregularities and take appropriate follow-up action on the basis of these reports. The supervisory board should monitor the management board in this task.
Principle 2.7 Preventing conflicts of interest	Any form of conflict of interest between the company and the members of its management board or supervisory board should be prevented. To avoid conflicts of interest, adequate measures should be taken. The supervisory board is responsible for the decision-making on dealing with conflicts of interest regarding management board members, supervisory board members and majority shareholders in relation to the company.

Principle 2.8 Takeover situations	In the event of a takeover bid for the company's shares or for the depositary receipts for the company's shares, in the event of a private bid for a business unit or a participating interest, where the value of the bid exceeds the threshold referred to in Section 2:107a(1)(c) of the Dutch Civil Code and/or in the event of other substantial changes in the structure of the organisation, both the management board and the supervisory board should ensure that the stakeholder interests concerned are carefully weighed and any conflict of interest for supervisory board members or management board members is avoided. The management board and the supervisory board should be guided in their actions by the interests of the company and its affiliated enterprise.

Chapter 3: Remuneration:	
Principle 3.1 Remuneration policy – management board	The remuneration policy applicable to management board members should be clear and understandable, should focus on long-term value creation for the company and its affiliated enterprise and take into account the internal pay ratios within the enterprise. The remuneration policy should not encourage management board members to act in their own interest, nor to take risks that are not in keeping with the strategy formulated and the risk appetite that has been established. The supervisory board is responsible for formulating the remuneration policy and its implementation.
Principle 3.2 Determining management board remuneration	The supervisory board should determine the remuneration of the individual members of the management board, within the limits of the remuneration policy adopted by the general meeting. The remuneration committee should prepare the supervisory board's decision-making regarding the

	determination of remuneration. The inadequate performance of duties should not be rewarded.
Principle 3.3 **Remuneration – supervisory board**	The supervisory board should submit a clear and understandable proposal for its own appropriate remuneration to the general meeting. The remuneration of supervisory board members should promote an adequate performance of their role and should not be dependent on the results of the company.
Principle 3.4 **Accountability for implementation of remuneration policy**	In the remuneration report, the supervisory board should render account of the implementation of the remuneration policy in a transparent manner. The report should be posted on the company's website.

Chapter 4: The General Meeting	
Principle 4.1 **The general meeting**	The general meeting should be able to exert such influence on the policies of the management board and the supervisory board of the company that it plays a fully-fledged role in the system of checks and balances in the company. Corporate governance requires the fully-fledged participation of shareholders in the decision-making in the general meeting.
Principle 4.2 **Provision of information**	The management board and the supervisory board should ensure that the general meeting is adequately provided with information.
Principle 4.3 **Casting votes**	Participation of as many shareholders as possible in the general meeting's decision-making is in the interest of the company's checks and balances. The company should, in so far as possible, give shareholders the opportunity to vote by proxy and to communicate with all other shareholders.
Principle 4.4 **Issuing depositary receipts for shares**	Depositary receipts for shares can be a means of preventing a majority (including a chance majority) of shareholders from

	controlling the decision-making process as a result of absenteeism at a general meeting.

Chapter 5: One-Tier Governance Structure	
Principle 5.1 **One-tier governance structure**	The composition and functioning of a management board comprising both executive and non-executive directors must be such that the supervision by non-executive directors is properly carried out and independent supervision can be assured.

ANNEXURE H: King IV Report on Corporate Governance for South Africa 2016 principles

Below are the principles as contained in King IV (IoDSA, 2016).

1. The governing body should lead ethically and effectively.
2. The governing body should govern the ethics of the organisation in a way that supports the establishment of an ethical culture.
3. The governing body should ensure that the organisation is and is seen to be, a responsible corporate citizen.
4. The governing body should appreciate that the organisation's core purpose, its risks and opportunities, strategy, business model, performance and sustainable development are all inseparable elements of the value creation process.
5. The governing body should ensure that reports issued by the organisation enable stakeholders to make informed assessments of the organisation's performance and its short-, medium- and long-term prospects.
6. The governing body should serve as the focal point and custodian of corporate governance in the organisation.
7. The governing body should comprise the appropriate balance of knowledge, skills, experience, diversity and independence for it to discharge its governance role and responsibilities objectively and effectively.
8. The governing body should ensure that its arrangements for delegation within its own structures promote independent judgment and assist with balance of power and the effective discharge of its duties.
9. The governing body should ensure that the evaluation of its own performance and that of its committees, its chair and its individual members, supports continued improvement in its performance and effectiveness.
10. The governing body should ensure that the appointment of and delegation to, management contribute to role clarity and the effective exercise of authority and responsibilities.

11. The governing body should govern risk in a way that supports the organisation in setting and achieving its strategic objectives.
12. The governing body should govern technology and information in a way that supports the organisation setting and achieving its strategic objectives.
13. The governing body should govern compliance with applicable laws and adopted, non-binding rules, codes and standards in a way that supports the organisation being ethical and a good corporate citizen.
14. The governing body should ensure that the organisation remunerates fairly, responsibly and transparently so as to promote the achievement of strategic objectives and positive outcomes in the short, medium and long term.
15. The governing body should ensure that assurance services and functions enable an effective control environment and that these support the integrity of information for internal decision-making and of the organisation's external reports.
16. In executing its governance role and responsibilities, the governing body should adopt a stakeholder-inclusive approach that balances the needs, interests and expectations of material stakeholders in the best interests of the organisation over time.
17. The governing body of an institutional investor organisation should ensure that responsible investment is practised by the organisation to promote the corporate governance and the creation of value by the companies in which it invests (IoDSA, 2016).

ANNEXURE I: Comparison between the UK Audit Firm Governance Code and King IV

A desktop study was conducted to compare the only current code for auditing firms – the UK's Audit Firm Governance Code – with the King IV Code that currently exists in South Africa. This comparison was used to identify the Principles and Values which were included in the questionnaire that was sent to the auditing firms (IoDSA, 2016; FRC, 2016).

UK Audit Firm Governance Code	King IV
A Leadership	
A.1 Owner accountability principle The management of a firm should be accountable to the firm's owners and no individual should have unfettered powers of decision.	**Principle 6:** The governing board (GB) should serve as the focal point and custodian of corporate governance in the organisation. **Principle 7:** The GB should comprise the appropriate balance of knowledge, skills, experience, diversity and independence. **Principle 9:** Evaluation of its own performance and that of its committees, its chair and its individual members, support continued improvement in its performance and effectiveness.
Provisions: A.1.1 The firm should **establish a board or equivalent governance structure,** with matters specifically reserved for its decision, to oversee the activities of the management team.	**Principle 6 Practice** The GB should exercise its leadership role by: • steering the organisation and setting its strategic direction; • approving policy and planning that give effect to the direction provided; • overseeing and monitoring the implementation and execution by management; and

A.1.2 The firm should state in its transparency report how its governance structures and management operate as well as their duties and the types of decisions they take. In doing so the firm should explain how its governance structure provide oversight of both the audit practice and the firm as a whole to ensure that the Code's purpose is achieved. If the management and/or governance of the firm rest at an international level, it should specifically set out how management and oversight of audit is undertaken and how the Code's purpose achieved in the UK. A.1.3 The firm should state in its transparency report the names and job titles of all members of the firm's governance structures and its management, how they are elected or appointed and their terms, length of service, meeting attendance in the year and relevant biographical details.	• ensuring accountability for organisational performance by, among others, reporting and disclosure. **Principle 7 Practice:** Disclosure with regards to the composition of the GB: • Satisfaction with regards to the appropriate mix of knowledge, skills, experience, diversity and independence on the GB. • The targets set for gender and race representation in the membership of the GB and progress made against these targets. • The categorisation of each member as executive or non-executive. • The categorisation of each non-executive member as independent or not and, when a non-executive member of the GB has been serving for longer than nine years, a summary of the views of the GB on the independence of the member. • The qualifications and experience of members. • Each member's period of service on the GB. • The age of each member. • Other GB and professional positions held by each member.

A.1.4 The members of a firm's governance structures and management should be subject to formal, rigorous and ongoing performance evaluation and, at regular intervals, members should be subject to re-election or re-selection.	• The reasons why any members of the GB have been removed, resigned or retired **Principle 9 practice:** • Evaluation of the GB's performance and that of its committees, its chair and its individual members. • The GB should appoint an INED member to lead the evaluation of the chair's performance if a lead independent is not in place. • A formal process should be followed every two years. • Every alternate year there should be a discussion regarding performance. • There should be a description of how the performance is evaluated. • Disclose the evaluation results. • Disclose if GB is satisfied with the results or what the improvement plan is.
A.2 Management principle A firm should have effective management which has responsibility and clear authority for running the firm.	**Principle 10:** Appointment of and delegation to, management.
Provision: A.2.1 Management should have terms of reference that include clear authority over the whole firm including its non-audit businesses	The delegation of authority framework addresses the authority to appoint executives who will serve as ex officio executive members of the GB and to make other executive appointments.

and these should be disclosed on the firm's website.	
B Values	
B.1 Professionalism principle A firm should perform quality work by exercising judgment and upholding values of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour in a way that properly takes the public interest into consideration and meets auditing and ethical standards.	**Principle 1:** The GB should lead ethically and effectively.
Provisions B.1.1 The firm's governance structures and management should establish and promote throughout the firm an appropriate culture, supportive of the firm's public interest role and long-term sustainability. This should be achieved in particular through the right tone from the top, through the firm's policies and practices and by management publicly committing themselves and the whole firm to quality work, the public interest and professional judgment and values. B.1.2 Firms should introduce KPIs on the performance of their governance system and report on performance against these in their transparency reports.	Members of the GB should individually and collectively cultivate the following characteristics and exhibit them in their conduct: **Integrity**, **Competence, Responsibility, Accountability, Fairness and Transparency.** Principle 9 as stated above.

B.1.3 The firm should have a code of conduct which it discloses on its website and requires everyone in the firm to apply. The board and INEDs should oversee compliance with it.	**Principle 2 Practice:**
	The GB should:
	• Assume responsibility for the governance of ethics and approve codes of conduct and ethics policies.
	• Ensure that codes of conduct and ethics policies:
	  • encompass the organisation's interaction with both internal and external stakeholders and the broader society; and
	  • address the key ethical risks of the organisation.
	• Employees and other stakeholders should be able to familiarise themselves with the codes of conduct and ethics policies.

B.2 Governance principle A firm should publicly commit itself to this Audit Firm Governance Code.	• Not applicable, as there is no Audit Firm Governance Code in South Africa. • King IV only makes reference to compliance to the Constitution of South Africa (including the Bill of Rights), the law, leading standards and adherence to its own codes of conduct and policies in Principle 3. • Principle 13 makes reference to the compliance with applicable laws and adopted, non-binding rules, codes and standards.
Provision	**N/A**

B.2.1 The firm should incorporate the principles of this Audit Firm Governance Code into an internal code of conduct.	
B.3 Openness principle A firm should maintain a culture of openness which encourages people to consult and share problems, knowledge and experience in order to achieve quality work in a way that properly takes the public interest into consideration.	Principle 16 refers to applying a stakeholder inclusive approach. **Principle 16 practice:** • The GB should encourage proactive engagement with shareholders, including engagement at the annual general meeting (AGM). • All directors should be available at the AGM. • The GB should ensure that shareholders are equitably treated and the interests of minority shareholders are protected. • The minutes of the AGMs of listed companies should be made publicly available.
C INEDs	
C.1 Involvement of INEDs principle A firm should appoint INEDs to the governance structure who through their involvement collectively enhance the firm's performance in meeting the purpose of the Code.	**Principle 7:** The GB should comprise the appropriate balance of knowledge, skills, experience, diversity and independence.
Provisions C.1.1 INEDs should number at least three and be in the majority on a body that oversees public interest matters; and/or be members of other relevant governance structures within the	**Principle 7 practice:** Comprise of a majority of non-executive members, most of whom should be independent.

firm. They should also meet as a separate group to discuss matters relating to their remit. They should have full visibility of the entirety of the business but should pay particular attention to and report on risks to audit quality and how they are addressed. If a firm considers that having three INEDs is inappropriate given its size or number of public company clients, it should explain this in its transparency report and ensure a minimum of two at all times. Where the firm adopts an international approach to its management it should have at least three INEDs with specific responsibility and relevant experience to focus on the UK business and to take part in governance arrangements for this market; or explain why it regards a smaller number to be more appropriate, in which event there should be a minimum of two.	
C.1.2 The firm should disclose on its website and in its transparency report information about the appointment, retirement and resignation of INEDs; their remuneration; their duties and the arrangements by which they discharge those duties; and the obligations of the firm to support them. The firm should report on why it has chosen to position its INEDs in the way it has (for example, as members of the main Board or on a public interest committee). The firm should also	Disclosure with regards to the composition of the GB: • Satisfaction with regards to the appropriate mix of knowledge, skills, experience, diversity and independence on the GB; • The targets set for gender and race representation in the membership of the GB and progress made against these targets; • The categorisation of each member as executive or non-executive;

disclose on its website the terms of reference and composition of any governance structures whose membership includes INEDs.	• The categorisation of each non-executive member as independent or not and, when a non-executive member of the GB has been serving for longer than nine years, a summary of the views of the GB on the independence of the member; • The qualifications and experience of members; • Each member's period of service on the GB. • The age of each member; • Other GB and professional positions held by each member; and • The reasons why any members of the GB have been removed, resigned or retired.
C.1.3 The INEDs should report in the firm's transparency report on how they have worked to meet the purpose of the Code defined as: • Promoting audit quality; • Helping the firm secure its reputation more broadly, including in its non-audit businesses; and • Reducing the risk of firm failure.	Transparency reports are not mandatory in South Africa and not all auditing firms issue transparency reports. The Big Four auditing firms do have transparency reports. However, disclosure is very limited in this regard. C1.3 is not in the King IV principles.
C.1.4 INEDs should have regular contact with the Ethics Partner, who should have a reporting line to them under the ethical standards.	C1.4 is not in the King IV principles.
C.2 Characteristics of INEDs principle	**Principle 7 practice (characteristics of independence)**

The INEDs' duty of care is to the firm. They should command the respect of the firm's owners and collectively enhance shareholder confidence by virtue of their independence, number, stature, experience and expertise. They should have a balance of relevant skills and experience including of audit and a regulated sector. At least one INED should have competence in accounting and/or auditing, gained for example from a role on an audit committee, in a company's finance function, as an investor or at an audit firm	A director is not independent if any of the following is applicable: • Significant provider of financial capital; • Participates in a share-based incentive scheme offered by the company; • Owns securities in the company; • Is an executive manager during the preceding three financial years, or is a related party to such executive manager; • Was the designated external auditor, or a key member of the audit team during the preceding three financial years; • Is a significant or ongoing professional advisor to the organisation; • Is a significant customer of, or supplier to the organisation; • Is a member of the GB or the executive management of another organisation which is a related party to the organisation; or • Is entitled to remuneration contingent on the performance of the organisation.
Provision C.2.1 The firm should state in its transparency report its criteria for assessing the impact of INEDs on the firm's independence as auditors and their independence from the firm and its owners.	Not in King IV.
C.3 Rights and responsibilities of INEDs principle	Nothing provided in King IV.

INEDs of a firm should have rights consistent with their role including a right of access to relevant information and people to the extent permitted by law or regulation and a right to report a fundamental disagreement regarding the firm to its owners and, where ultimately this cannot be resolved and the INED resigns, to report this resignation publicly.	
Provisions C.3.1 Each INED should have a contract for services setting out their rights and duties. C 3.2 INEDs should be appointed for specific terms and any term beyond nine years should be subject to particularly rigorous review and explanation. C 3.3 The responsibilities of an INED should include, but not be limited to, oversight of the firm's policies and processes for: • Promoting audit quality; • Helping the firm secure its reputation more broadly, including in its non-audit businesses; and • Reducing the risk of firm failure. C.3.4 The firm should ensure that appropriate indemnity insurance is in place in respect of legal action against any INED in respect of their work in that role. C.3.5 The firm should provide each INED with sufficient resources to undertake their duties including having access to independent professional advice at the firm's expense	**Principle 7 practice** A non-executive member of the GB may continue to serve, in an independent capacity, for longer than nine years. No detail on this in King IV, as it is not specifically focused on auditing firms.

where an INED judges such advice necessary to discharge their duties. C.3.6 The firm should establish and disclose on its website, procedures for dealing with any fundamental disagreement that cannot otherwise be resolved between the INEDs and members of the firm's management team and/or governance structures.	
D Operations	
D.1 Compliance principle A firm should comply with professional standards and applicable legal and regulatory requirements. Operations should be conducted to promote audit quality and the reputation of the firm. The INEDs should be involved in the oversight of operations.	King IV does not make specific reference to audit quality and standards as it is not a code for auditing firms. It does make reference to the governance of compliance with applicable laws and adopted, non-binding rules, codes and standards in Principle 13, as stated above.
Provisions D.1.1 The firm should establish policies and procedures for complying with applicable legal and regulatory requirements and international and national standards on auditing, quality control and ethics, including auditor independence. D.1.2 The firm should establish policies and procedures for individuals signing group audit reports to comply with applicable standards on auditing dealing with group audits including reliance on other auditors whether from the same network or otherwise. D.1.3 The firm should state in its transparency report how it applies policies and procedures	No specific reference to audit and audit quality.

for managing potential and actual conflicts of interest. D.1.4 The firm should take action to address areas of concern identified by audit regulators in relation to the firm's audit work.	
D.2 Risk management principle A firm should maintain a sound system of internal control and risk management over the operations of the firm as a whole to safeguard the firm and reassure stakeholders.	**Principle 11:** The governance of risk.
Provisions D.2.1 The firm should, at least annually, conduct a review of the effectiveness of the firm's system of internal control. INEDs should be involved in the review which should cover all material controls, including financial, operational and compliance controls and risk management systems as well as the promotion of an appropriate culture underpinned by sound values and behaviour within the firm. D.2.2 The firm should state in its transparency report that it has performed a review of the	**Principle 11 practice** The GB should consider: • The opportunities and associated risks to be considered when developing strategy; • The potential positive and negative effects of the same risk on the achievement of organisational objectives; • The organisation's risk appetite; and • The limit of the potential loss that the organisation can tolerate. The GB should delegate to management the responsibility to implement and execute effective risk management. The GB should receive periodic independent assurance on the effectiveness of risk management. The nature and extent of the risks and opportunities they are willing to take should be disclosed.

effectiveness of the system of internal control, summarise the process it has applied and confirm that necessary actions have been or are being taken to remedy any significant failings or weaknesses identified from that review. It should also disclose the process it has applied to deal with material internal control aspects of any significant problems disclosed in its financial statements or management commentary.	
D.2.3 The firm should carry out a robust assessment of the principal risks facing it, including those that would threaten its business model, future performance, solvency or liquidity. This should reference specifically the sustainability of the audit practice within the UK.	King refers to risk assessment as stated above.
D.3 People management principle A firm should apply policies and procedures for managing people across the whole firm that support its commitment to the professionalism, openness and risk management principles of the Audit Firm Governance Code.	No information on this in King IV, as the code is not specifically for auditing firms.
Provisions D.3.1 The firm should disclose on its website how it supports its commitment to the professionalism, openness and risk management principles of the Audit Firm Governance Code through recruitment, development activities, objective setting, performance evaluation, remuneration,	No information on this in King IV, as the code is not specifically for auditing firms.

progression, other forms of recognition, representation and involvement. D.3.2 INEDs should be involved in reviewing people management policies and procedures, including remuneration and incentive structures, to ensure that the public interest is protected.	
D.4 Whistleblowing principle A firm should establish and apply confidential whistleblowing policies and procedures across the firm which enable people to report, without fear, concerns about the firm's commitment to quality work and professional judgment and values in a way that properly takes the public interest into consideration. The INEDs should be satisfied that there is an effective whistleblowing process in place.	No information of whistleblowing in King IV.
Provision D.4.1 The firm should report to INEDs on issues raised under its whistleblowing policies and procedures and disclose those policies and procedures on its website.	No information of whistleblowing in King IV.
E Reporting	
E.1 Internal reporting principle The management of a firm should ensure that members of its governance structures, including owners and INEDs, are supplied with information in a timely manner and in a form and of a quality appropriate to enable them to discharge their duties.	The King IV Code refers to disclosure throughout the Code. King IV encourages transparent and meaningful reporting to stakeholders. Principle 5 specifically refers to integrated reporting and states that the GB should ensure

	that reports issued by the organisation enable stakeholders to make informed assessments of the organisation's performance and its short, medium and long-term prospects.
E.2 Governance reporting principle A firm should publicly report how it has applied in practice each of the principles of the Audit Firm Governance Code and make a statement on its compliance with the Code's provisions or give a considered explanation for any non-compliance.	Entities listed on the JSE are required to disclose how they have applied King IV.
Provisions E.2.1 The firm should publish on its website an annual transparency report containing the disclosures required by Code Provisions A.1.2, A.1.3, B1.2, C.2.1, D.1.3, D.2.2, E.2.2 and E.3.1. E2.2 In its transparency report the firm should give details of any additional provisions from the UK Corporate Governance Code which it has adopted within its own governance structure.	King IV does not make reference to transparency reports, as the Code is not specifically for auditing firms. The IRBA has requested that auditing firms issue a transparency report, however, in South Africa this is not yet compulsory.
E.3 Transparency principle A firm should publish on an annual basis in its transparency report a commentary on the firm's performance, position and prospects.	The GB should ensure that the following information is published on the organisation's website, on other platforms or through other media as is appropriate for access by stakeholders: • Corporate governance disclosures required in terms of the Code; • Integrated reports; and

	• Annual financial statements and other external reports.
Provisions E.3.1 The firm should confirm that it has carried out a robust assessment of the principal risks facing the audit firm, including those that would threaten its business model, future performance, solvency or liquidity. The firm should describe those risks and explain how they are being managed or mitigated. E.3.2 The transparency report should be fair, balanced and understandable in its entirety.	Principle 11 addresses the governance of risk, as stated above, as well as risk disclosure. No information on transparency reports in King IV.
E.4 Reporting quality principle A firm should establish formal and transparent arrangements for monitoring the quality of external reporting and for maintaining an appropriate relationship with the firm's auditors.	**Principle 8:** Delegation should promote independent judgment and assist with balance of power and the effective discharge of its duties. This principle discusses the appointment of an audit committee.
Provision E.4.1 The firm should establish an audit committee and disclose on its website information on the committee's membership and terms of reference which should deal clearly with its authority and duties, including its duties in relation to the appointment and independence of the firm's auditors. On an annual basis, the audit committee should publish a description of its work and how it has discharged its duties.	**Principle 8 Practice:** It is a statutory requirement to have an audit committee for some organisations. The audit committee provides oversight of: • The effectiveness of the organisation's assurance functions and services; and • The integrity of the annual financial statements. All members of the audit committee should be independent, non-executive members of the GB.

	The GB should appoint an independent, non-executive member to chair the audit committee. The audit committee should meet annually with the internal and external auditors respectively, without management being present. A statement should be disclosed as to whether the audit committee is satisfied that the external auditor is independent of the organisation.
E.5 Financial statements principle A firm should publish audited financial statements prepared in accordance with a recognised financial reporting framework such as International Financial Reporting Standards or UK GAAP. These statements should be clear and concise.	**Principle 5:** The GB should ensure that reports issued by the organisation enable stakeholders to make informed assessments of the organisation's performance and its short-, medium- and long-term prospects.
Provisions E.5.1 The firm should explain who is responsible for preparing the financial statements and the firm's auditors should make a statement about their reporting responsibilities, preferably in accordance with the extended audit report standards. E.5.2 The firm should state whether it considers it appropriate to adopt the going concern basis of accounting and identify any material uncertainties to its ability to continue to do so, with supporting assumptions or qualifications as necessary.	The GB should oversee that reports such as the annual financial statements, sustainability reports, social and ethics committee reports or other online or printed information or reports are issued as necessary, to comply with legal requirements and/or to meet the legitimate and reasonable information needs of material stakeholders.

F Dialogue	
F.1 Firm dialogue principle A firm should have dialogue with listed company shareholders, as well as listed companies and their audit committees, about matters covered by the Audit Firm Governance Code to enhance mutual communication and understanding and ensure that it keeps in touch with shareholder opinion, issues and concerns.	King IV does recommend a stakeholder-inclusive approach in Principle 16.
Provision F.1.1 The firm should disclose on its website its policies and procedures, including contact details, for dialogue about matters covered by the Audit Firm Governance Code with listed company shareholders and listed companies. It should also report on the dialogue it has had during the year. These disclosures should cover the nature and extent of the involvement of INEDs in such dialogue.	**Principle 16 practice:** • The GB should encourage proactive engagement with shareholders, including engagement at the AGM. • All directors should be available at the AGM. • The GB should ensure that shareholders are equitably treated and the interests of minority shareholders are protected. • The minutes of the AGMs of listed companies should be made publicly available.
F.2 Shareholder dialogue principle Shareholders should have dialogue with auditing firms to enhance mutual communication and understanding.	The designated partner of the external audit firm attends the AGM.
F.3 Informed voting principle Shareholders should have dialogue with listed companies on the process of recommending the appointment and re-appointment of auditors and should make considered use of votes in relation to such recommendations.	The audit committee provides oversight of the effectiveness of the organisation's assurance functions and services. No specific reference is made to the re-appointment of the auditors.

IoDSA (2016); FRC (2016)

When assessing the above comparison, it is clear that the King IV Code does make reference to almost all of the principles that are in the UK Audit Firm Governance Code. As that the King Codes are based on the UK Corporate Governance Codes (previously, the Cadbury Report), the UK Audit Firm Code is used in this study as a basis and benchmark for developing a corporate governance code specifically for auditing firms in South Africa. The King IV Code does contain more principles which are not specifically addressed in the UK Audit Firm Code and these are considered during the development phase. The questionnaire was formulated based on the information provided above.

ANNEXURE J: Ethical clearance certificate

UNIVERSITY OF JOHANNESBURG

SCHOOL OF ACCOUNTING RESEARCH ETHICS COMMITTEE (SAREC)

Dear Rozanne

ETHICAL APPROVAL GRANTED FOR RESEARCH PROJECT

Decision: Clearance granted

This letter serves to confirm that the proposed research project indicated in the table below, has been reviewed by the School of Accounting Research Ethics Committee at the University of Johannesburg. Ethical clearance is granted for 5 years, from 10 September 2020 to 9 September 2025.

Applicant	Mrs RJ Smith
Supervisor	Prof B Marx
Staff number	720016433
Title of Research **PhD Auditing**	The application of corporate governance in large and medium sized South African auditing firms
Decision date at meeting	8 September 2020
Reviewers	M Bornman, M Hlobo & M Wassermann
Ethical clearance code	SAREC20200908/01
Rating of application	CODE 01

CODE 01 - Approved CODE 02 - Approved with suggestions without re-submission

CODE 03 - Referred back CODE 04 - Disapproved, cannot re-submit

The researcher/s may now commence with the study providing that:

1. The researcher will ensure that the project adheres to ethical research requirements;
2. The researcher will be conducting the study as set out in the approval application;
3. The researcher will ensure that the project adheres to all applicable legislation, scopes of practice, professional codes of conduct and scientific standards as it pertains to the field of study;
4. The researcher will bring to the attention of the research ethics committee any proposed changes, concerns that arise and unexpected ethical management issues;
5. Any changes that can affect the study-related risks for participants or researchers must be reported to the committee in writing;
6. All relevant permission required to access data, organisations, etc. has been obtained;
7. No fieldwork activities may continue after the ethical clearance has expired. A request for an extension of ethical clearance can be made in writing to the REC.

Prof M Bornman

Chairperson: SAREC

Email: mbornman@uj.ac.za

Telephone: 011 559 3873

ANNEXURE K: Cover letter from supervisor – Professor Ben Marx

COVER LETTER FROM PROFESSOR BEN MARX TO THE CEO OF THE AUDIT FIRM

To: <PERSONALISED NAME>	From: ROZANNE SMITH
Date: SEPTEMBER 2020	Subject: QUESTIONNAIRE: AUDIT FIRM GOVERNANCE STRUCTURES

Corporate governance codes for corporate entities are well established worldwide. However, corporate governance codes specifically applicable to auditing firms are rare and exist in only one country – the United Kingdom. The recent high-profile corporate failures which have taken place overseas and in South Africa highlight the lack of sound governance that often exist in auditing firms. These corporate failures – which are often seen as audit failures – cast a very negative light on the auditing profession as whole. This study is being undertaken to develop sound corporate governance practices for South African auditing firms, to 'set the tone at the top' in order to restore public trust in the profession. Specific focus is placed on the oversight board of auditing firms and its governance.

The research is being conducted by Rozanne Smith, an academic at the University of Johannesburg and is supported by the South African Auditing Profession Trust Initiative (SAAPTI). It forms part of a PhD study on the corporate governance structures of the top 10 auditing firms in South Africa that have 20 or more partners, as classified by the IRBA.

Your input as a leader in corporate South Africa is critical and will be of immense value to the success of the study.
Should you have any objection to completing the questionnaire, please state your reason and return the questionnaire for control purposes.

We thank you in advance of your co-operation

Professor Ben Marx

MCom, DCom, CA(SA)

Study leader

Your response is vital to the success of this study

INSTRUCTIONS
1. The questionnaire should be completed electronically. a. Click on the following link and follow the prompts to complete the questionnaire. b. Mark your answer in the appropriate box with a cross (X) by clicking in the appropriate block with your mouse or type the relevant information as requested. c. Should you wish to change your answer in any of the boxes, simply click on that box again to clear it and re-select your answer. d. Once you have completed the questionnaire, please click on 'submit'. e. *Google form link to be included here.* 2. Please do not hesitate to supply additional information that might be of relevance to this research. 3. The due date for the completed questionnaire is **30 September 2020.** 4. **Should you wish to contact Rozanne Smith, you can do so on 072 246 9244 or rozannes@uj.ac.za.** 5. All information will be treated as confidential and will only be used to produce aggregate results. 6. Should you wish to receive a copy of the study and findings, please indicate so on the questionnaire.
Your co-operation is greatly appreciated **Thank you in advance**

ANNEXURE L: Cover letter from SAAPTI

COVER LETTER FROM MR DION SHANGO TO THE CEO OF THE AUDIT FIRM

To: <PERSONALISED NAME>	From: ROZANNE SMITH
Date: SEPTEMBER 2020	Subject: QUESTIONNAIRE: AUDIT FIRM GOVERNANCE STRUCTURES

I would be grateful if you could take a few minutes to complete the attached questionnaire on corporate governance practices at auditing firms, with specific reference to the governing body. The research is extremely relevant given the recent corporate failures in South Africa that have involved auditing firms and the governance at the auditing firms. The research results will add to future developments of the King Code and may possibly be included as a sector supplement to future King Code iterations. As a business leader and CEO of an auditing firm, your input is essential.

The research is undertaken by Rozanne Smith, an academic at the University of Johannesburg and is supported by the South African Auditing Profession Trust Initiative (SAAPTI). Rozanne is currently completing her PhD in Auditing. The study is supervised by Professor Ben Marx, a well-known professor, with numerous publications on auditing and corporate governance.

The questionnaire should not take longer than 20 minutes. As part of the nine auditing firms involved in the study, your response is critical to the success of the research.

The questionnaire can be completed by clicking on this link: *Link to be included here*. Once you have completed the questionnaire, please click on ‘submit’.

Should you wish to contact Rozanne Smith, you can do so on 072 246 9244 or rozannes@uj.ac.za. Your co-operation is greatly appreciated.

Dion Shango

Chairman of SAAPTI

ANNEXURE M: Checklist data collection tool

Control sheet for the analysis of the transparency reports

Name of the company or firm: (This will only be used should additional information be required after the completion of the questionnaire. The names of the auditing firm will not be made public in the research and all information will be treated as confidential and only reported on in aggregate).

[Yes=Y; No=N]

		Y	**N**
1	**Does the auditing firm issue a transparency report?**		
Comments:			

		Y	**N**
2	**If 'YES' to question number '1', where is the transparency report published?**		
2.1	Company website?		
2.2	Emailed the company and requested it?		
Comments:			

		Y	**N**
3	**Does the auditing firm issue an integrated report?**		
Comments:			

		Y	N
4	**If 'YES' to question number '3', where is the integrated report published?**		
4.1	On the company website?		
4.2	Had to email the company and request it?		
Comments:			

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR).		**TR**		**IR**	
		Y	**N**	**Y**	**N**
5.	**Does the audit firm disclose information about the Board of Directors?**				
Comments:					

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR).		**TR**		**IR**	
		Y	**N**	**Y**	**N**
6.	**Does the audit firm disclose information about the Oversight Board?**				
Comments:					

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR).		**TR**	**IR**
7.	**With regards to the composition of the <u>Board of Directors</u>, what information is disclosed on the composition of the Board of Directors?**		
7.1	Number of members		
7.2	Number of Executive directors		
7.3	Number of Non-executive directors		

7.4	Number of INED directors		
7.5	**Race (number of members)**		
	a. Black		
	b. Coloured		
	c. Indian		
	d. White		
7.6	**Gender (number of members)**		
	a. Male		
	b. Female		
Comments:			

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR).		**TR**	**IR**
8.	**With regards to the composition of the <u>Oversight Board</u>, what information is disclosed on the composition of the Oversight Board?**		
8.1	Number of members		
8.2	Number of Executive directors		
8.3	Number of Non-executive directors		
8.4	Number of INED directors		
8.5	**Race (number of members)**		
	a. Black		
	b. Coloured		
	c. Indian		
	d. White		
8.6	**Gender (number of members)**		
	a. Male		
	b. Female		
Comments:			

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR).		TR		IR	
		Y	**N**	**Y**	**N**
9.	**From the information disclosed on the <u>Board of Directors</u>, does the <u>Board of Directors</u> consist of**:				
9.1	A majority of INED directors?				
9.2	At least three INED directors?				
9.3	If your answer in 6.2 is "no", do you disclose the reason for not having at least three INED directors on the Board of Directors?				
9.4	A majority of INED directors whom are members of other relevant governance structures in the firm?				
9.5	INED directors who have a balance of relevant skills and experience in audit?				
9.6	At least one INED director who has competence in accounting and/or auditing?				
Comments:					

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR) disclosure.		TR		IR	
		Y	**N**	**Y**	**N**
10.	**From the information disclosed on the <u>Oversight Board</u>, does the <u>Oversight Board</u> consist of**:				
10.1	A majority of INED directors?				
10.2	At least three INED directors?				

10.3	If your answer in 10.2 is “no”, do you disclose the reason for not having at least three INED directors on the Oversight Board?				
10.4	A majority of INED directors whom are members of other relevant governance structures in the firm?				
10.5	INED directors who have a balance of relevant skills and experience in audit?				
10.6	At least one INED director who has competence in accounting and/or auditing?				
Comments:					

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR) disclosure.		**TR**		**IR**	
		Y	**N**	**Y**	**N**
11.	**With regards to the disclosure of information pertaining to the <u>Board of Directors</u> does the transparency report or the integrated report:**				
11.1	State how the audit firm’s Board of Directors operate their duties?				
11.2	State what type of decisions are made by the Board of Directors?				
11.3	State the names and job titles of all members of the Board of Directors?				
11.4	State how the members of the Board of Directors was elected or appointed?				
11.5	State the terms of the members of the Board of Directors?				

11.6	State the length of service of the members of the Board of Directors?				
11.7	State the meeting attendance in the year of the members of the Board of Directors?				
11.8	State any biographical details of the members of the Board of Directors?				
11.9	Include information on the appointment, retirement and resignation of INED directors?				
11.10	Include information on the remuneration of the INED directors?				
11.11	Include information on the duties of the INED directors?				
11.12	Include arrangements by which the INED directors discharge their duties?				
11.13	Include how the supports the INED directors in discharging their duties?				
11.14	Explain how the audit firm has positioned its INED directors (on the Board of Directors or the Oversight Board)?				
11.15	State the criteria for assessing the impact of INED directors on the firm's independence as auditors and their independence from the firm and its owners?				
Comments:					

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR).		**TR**		**IR**	
		Y	**N**	**Y**	**N**

12.	**With regards to the disclosure of information pertaining to the <u>Oversight Board</u> does the transparency report or the integrated report:**				
12.1	State how the audit firm's Oversight Board operate their duties?				
12.2	State what type of decisions are made by the Oversight Board?				
12.3	State the names and job titles of all members of the Oversight Board?				
12.4	State how the members of the Oversight Board was elected or appointed?				
12.5	State the terms of the members of the Oversight Board?				
12.6	State the length of service of the members of the Oversight Board?				
12.7	State the meeting attendance in the year of the members of the Oversight Board?				
12.8	State any biographical details of the members of the Oversight Board?				
12.9	Include information on the appointment, retirement and resignation of INED directors?				
12.10	Include information on the remuneration of the INED directors?				
12.11	Include information on the duties of the INED directors?				
12.12	Include arrangements by which the INED directors discharge their duties?				
12.13	Include how the supports the INED directors in discharging their duties?				

12.14	Explain how the audit firm has positioned its INED directors (on the Board of Directors or the Oversight Board)?				
12.15	State the criteria for assessing the impact of INED directors on the firm's independence as auditors and their independence from the firm and its owners?				
Comments:					

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR).		**TR**		**IR**	
		Y	**N**	**Y**	**N**
13.	**With regards to the disclosure of information pertaining to <u>risk management</u>, does the transparency report or the integrated report:**				
13.1	Disclose that a review was performed on the effectiveness of the system of internal control?				
13.2	Disclose which process was applied to perform a review on the effectiveness of the system of internal control?				
13.3	Disclose what weaknesses were identified in the review on the effectiveness of the system of internal control?				
13.4	Disclose what actions will be taken to deal with weaknesses identified in the review of the system of internal control?				
13.5	Disclose on the audit firm's website how the firm will support its commitment to the professionalism, openness and risk management?				
13.6	Disclose on the auditing firms' website the whistleblowing policies and procedures?				
Comments:					

		TR		IR	
This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR).					
		Y	**N**	**Y**	**N**
14.	**With reference to disclosure in the transparency report and the integrated report, does your auditing firm:**				
14.1	State how the firm applies policies and procedures for managing potential and actual conflicts of interest?				
14.2	Include a commentary on the firm's performance, position and prospects?				
14.3	Include fair and balanced information?				
14.4	Explain everything in an understandable manner?				
Comments:					

15	**With regards to disclosure on the audit firm's website, is the following information disclosed on the audit firm's website**	**Y**	**N**
15.1	Discloses on its website its policies and procedures for dialogue with listed company shareholders and listed companies?		
15.2	Discloses the nature and extent of the involvement of the INED director in the dialogues?		
15.3	Disclose its code of conduct on the audit firm website?		
15.4	Disclose on the website to whom the code of conduct is applicable to?		
15.5	Disclose on its website, procedures for dealing with any fundamental disagreement between the INEDs and members of the firm's management team and/or governance structures?		
Comments:			

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR).		TR		IR	
		Y	N	Y	N
16.	**Does the auditing firm disclose information on any of the following committees:**				
16.1	Audit committee				
16.2	Risk Committee				
16.3	Nomination Committee				
16.4	Remuneration Committee				
16.5	Ethics Committee				
Comments:					

		Y	**N**
17	**If the auditing firms has an audit committee, is it constituted according to the principles in King IV?**		
Comments:			

This question requires a response with regards to both, the Transparency Report (TR) and the Integrated Report (IR).		TR		IR	
		Y	N	Y	N
18.	**With reference to audited financial statements, does the auditing firm:**				
18.1	Publish audited financial statements?				
18.2	Publish audited financial statements that are prepared in accordance with the recognised financial reporting framework?				

18.3	Publish audited financial statements that are clear and concise?				
18.4	Explain who is responsible for preparing the financial statements				
Comments:					

ANNEXURE N: Questionnaire data collection tool

QUESTIONNAIRE TO THE CHIEF EXECUTIVE OFFICER OF THE AUDIT FIRM

Your response is vital to the success of this study

INSTRUCTIONS
1. The questionnaire should be completed electronically. a. Click on the following link and follow the prompts to complete the questionnaire. b. Mark your answer in the appropriate box with a cross (X) by clicking in the appropriate block with your mouse or type the relevant information as requested. c. Should you wish to change your answer in any of the boxes, simply click on that box again to clear it and re-select your answer. d. Once you have completed the questionnaire, please click on 'submit'. e. *Google form link to be included here.* 2. Please do not hesitate to supply additional information that might be of relevance to this research. 3. The due date for the completed questionnaire is **30 September 2020.** 4. All information will be treated as confidential and will only be used to produce aggregate results. 5. Should you wish to receive a copy of the study and findings, please indicate so on the questionnaire.

Your co-operation is greatly appreciated
Thank you in advance

Should you wish to contact Rozanne Smith, you can do so on 072 246 9244 or rozannes@uj.ac.za**.**

Introduction and background

This questionnaire forms part of a PhD study entitled The Application of Corporate Governance in Large and Medium Sized South African Auditing Firms. An analysis of the transparency reports of the largest auditing firms in South Africa revealed that there are differences in the legal structure and governance oversight structures of auditing firms.

Thus, auditing firms can be either a partnership or incorporated as a company.

For an audit firm that is incorporated as a company, all shareholders are directors and all directors have to be Registered Auditors (RA).

For auditing firms that are partnerships, all partners are directors and all directors have to be Registered Auditors (RA).

In both these types of structures, the audit firm elects directors to form an Executive Committee (EXCO) which is responsible for the day-to-day management of the firm.

It was also found that some auditing firms appoint an independent oversight structure. This body, which is not part of the day-to-day management of the firm, provides oversight of the EXCO and governance.

This questionnaire refers to both the EXCO and the oversight board. It is therefore important to understand how these structures are defined.

Please note that the questions below relate specifically to South Africa and not to global Executive Committees/Boards or global Oversight Boards.

The study focuses on governance and oversight and the structures used within auditing firms to ensure sound governance and oversight.

The study does not specifically focus on audit quality, although it is recognised that sound governance and oversight by an independent board should result in a high level of audit quality and public trust.

	Y	N
Do you provide consent that the data gathered in this questionnaire may be used for research purposes?		

Name of the firm: This will only be used should additional information be required after the completion of the questionnaire. The name of the auditing firm **will not** be made public in the research. All information will be treated as strictly confidential and only reported in aggregate.

The following questions are on the current practice at your audit firm. Please keep in mind that the questions relate specifically to South African boards/committees.

	Y	N
Does your audit firm currently have an EXCO?		
If yes, what is this board or committee named in your audit firm?		

	Y	N
Does your audit firm currently have an oversight board?		
If yes, what is this board or committee named in your audit firm?		
If “yes”, do you have independent members on the oversight board?		
If “no”, do you plan on appointing an oversight board in the near future?		
If “no”, why do you not plan on appointing an oversight board?		
If “no”, how do you ensure independence oversight within your audit firm?		

Please select the option(s) that are most applicable to your audit firm. Please click on the box which is relevant.

If your audit firm has an oversight board, does this board apply corporate governance principles as contained in King IV?	
Only some of the principles	
All of the principles	
None of the principles	
Comments:	

Are you of the opinion that the members of your EXCO and/or oversight board <u>understand</u>:	
Their role in corporate governance?	
The objective of practising good corporate governance?	
The value that corporate governance can add to the board of directors and/or the oversight committee?	
That they are the focal point and custodian of corporate governance in the organisation?	
The function and responsibilities of the board of directors and/or the oversight committee in corporate governance?	
Comments:	

Are you of the opinion that your EXCO is *effective* in discharging its responsibilities of <u>sound governance of risk</u> through:	**To a large extent**	**To a lesser extent**	**Totally ineffective**
Maintaining a sound system of internal control?			
Maintaining a sound system of risk management over the operations of the firm?			
Conducting an annual review of the effectiveness of the firm's system of internal control?			

INED directors reviewing all material controls in the audit firm?			
INED directors promoting an appropriate culture underpinned by sound values and behaviour in the firm?			
Disclosing in the transparency report that a review was performed of the effectiveness of the internal control system?			
Disclosing in the transparency report which process was applied to perform a review of the effectiveness of the internal control system?			
Disclosing in the transparency report what weaknesses were identified in the review of the effectiveness of the internal control system?			
Disclosing, in the transparency report what actions will be taken to deal with weaknesses identified in the review of the internal control system?			
Carrying out a robust assessment of the principal risks the audit firm is faced with?			
Describing the risks and explaining how they are being managed or mitigated?			
Applying policies and procedures for managing people across the whole firm?			
Disclosing, on the firm's website, how the firm will support its commitment to professionalism, openness and risk management?			
Establishing whistleblowing policies and procedures?			
Disclosing, on the firm's website, the whistleblowing policies and procedures?			
Reporting to the INED directors on issues raised under the whistleblowing policies and procedures?			
Comments:			

Please select the applicable answer by clicking on either Y [Yes] or N [No].

With reference to reports, does your auditing firm:	Y	N

Issue a transparency report on an annual basis?		
Issue an integrated report on an annual basis?		
Comments:		

	Y	N
With reference to disclosure in the transparency report, does your auditing firm:		
State how the firm applies policies and procedures to manage potential and actual conflicts of interest?		
Include a commentary on the firm's performance, position and prospects?		
Include fair and balanced information?		
Explain everything in an understandable manner?		
Disclose information on the corporate governance of the firm?		
Comments:		

	Y	N
With reference to the <u>corporate governance</u> of the auditing firm, in your opinion does your auditing firm:		
Have formal, rigorous and ongoing performance evaluations of the members of the governance structure?		
Introduce KPIs for the performance of their governance system?		
Disclose its code of conduct on the firm's website?		
Disclose on the website to whom the code of conduct is applicable?		
Ensure that appropriate indemnity insurance is in place in case of legal action against any INED member's work in that role?		
Disclose on its website procedures for dealing with any fundamental disagreement between the INEDs and members of the firm's management team and/or governance structures?		

Comply with professional standards and applicable legal and regulatory requirements?		
Operate in a way that promotes audit quality and the reputation of the firm?		
Establish policies and procedures for complying with applicable legal and regulatory requirements?		
Establish policies and procedures for individuals signing audit reports to comply with applicable standards?		
Establish policies and procedures for the reliance on work performed by other auditors, whether from the same network or otherwise?		
Take action to address areas of concern identified by audit regulators in relation to the firm's audit work?		
Supply members of its governance structures, including owners and INEDs, with information in a timely manner?		
Supply members of its governance structures, including owners and INEDs, with quality information to enable them to discharge their duties?		
Comments:		

	Y	N
With specific reference to the <u>financial statements</u> of the audit firm, does your firm:		
Publish audited financial statements?		
Publish audited financial statements that are prepared in accordance with the recognised financial reporting framework?		
Publish audited financial statements that are, in your opinion, clear and concise?		
Explain who is responsible for preparing the financial statements?		
Do auditors make a statement about their reporting responsibilities in accordance with the extended audit report standards?		

State whether it considers it appropriate to adopt the going concern basis of accounting and identify any material uncertainties to its ability to continue to do so, with supporting assumptions or qualifications as necessary.		
Comments:		

	Y	N
Does your audit firm:		
Have terms of reference/framework for EXCO for the delegation of authority?		
Have terms of reference/framework for EXCO that include clear authority over the whole firm, including its non-audit business?		
Disclose its terms of reference on the firm's website?		
Comments:		

	Y	N
With reference to an <u>audit committee</u>, does your auditing firm:		
Have an audit committee?		
Have an audit committee which monitors the quality of external reporting?		
Have an audit committee which maintains an appropriate relationship with the firm's auditors?		
Disclose on its website the audit committee's membership details?		
Have terms of reference for the audit committee?		
On an annual basis, publish a description of how the audit committee has discharged its duties?		
Have an audit committee which is constituted in accordance with the recommendations in the King IV Code of Corporate Governance?		
Comments:		

The 'Audit Firm Governance Code' in the UK is the only corporate governance code in the world which is specifically applicable to auditing firms. The questions below are derived from the UK Code and require your <u>expert opinion</u> on the development of a corporate governance oversight framework for South African auditing firms.

Please select the applicable answer by clicking on either Y [Yes] or N [No].

	Y	**N**
Are you of the opinion that there should be a corporate governance framework that regulates the governance of South African auditing firms?		
If yes, are you of the opinion that any of the following platforms should be used to guide audit firm governance?		
A Code of Corporate Governance, such as King IV?		
JSE		
Regulation or legislation?		
None of the above.		
If "no", why not?		

	Y	**N**
If a corporate governance framework should be developed to provide guidance to auditing firms, do you believe that an oversight board should have the responsibility of governance and oversight?		
If "no", why not?		

	Y	**N**
Do you think that the appointment of INED directors to the oversight board is important?		
If "no", why not?		

	Y	N
In your opinion, do you think that independent directors play an important role in governance and oversight within an audit firm?		
If "no", why not?		

	Y	N
Do you believe that an independent oversight board can add value to an audit firm?		
If "no", why not?		

	Y	N
Are you of the opinion that an oversight board of an audit firm should:		
Be properly constituted in terms of corporate governance codes such as King IV?		
Operate according to a well-formulated charter?		
Be provided with the necessary **authority** to be able to effectively discharge its responsibilities in terms of corporate governance?		
Be provided with the necessary **resources** to be able to effectively discharge its responsibilities in terms of corporate governance?		
Lead ethically?		
Lead effectively?		
Uphold values of objectivity?		
Take the public interest into consideration?		
Comply with auditing and ethical standards?		
Promote an appropriate ethical culture?		
Assist the audit firm in achieving an appropriate ethical culture?		
Oversee compliance with a code of conduct?		

Commit itself to a corporate governance code?		
Incorporate the principles of a corporate governance code into the internal code of conduct?		
Maintain a culture of openness which encourages people to share their problems, knowledge and experience?		
Provide oversight of both the audit practice and the firm as a whole?		
Comments:		

	Y	**N**
Are you of the opinion that an oversight board of an audit firm should consist of:		
A majority of INED directors?		
At least three INED directors?		
INED directors who oversee public interest matters?		
A majority of INED directors who are members of other relevant governance structures in the firm?		
INED directors who pay particular attention to and report on risk and audit quality?		
INED directors who command respect of the firm’s owners?		
INED directors who collectively enhance shareholder confidence by virtue of their independence, number, stature, experience and expertise?		
INED directors who have a balance of relevant skills and experience in audit?		
At least one INED director who has competence in accounting and/or auditing?		
Comments:		

	Y	**N**
Are you of the opinion that the INED directors who are appointed to the oversight board of an audit firm should:		
Have rights consistent with their role to the extent permitted by law or regulation?		

Have the right to access relevant information to the extent permitted by law or regulation?		
Have the right to access people to the extent permitted by law or regulation?		
Have a contract for their services, setting out their rights and duties?		
Be appointed for a specific term?		
Be subject to a rigorous review of independence in cases where their term extends beyond nine years?		
Be involved in reviewing people management policies and procedures (e.g. remuneration) to protect the public interest?		
<u>Have at least the following duties:</u>		
• Oversight of the firm's policies and procedures.		
• Helping the firm maintain its reputation (in audit and non-audit business).		
• Reduce the risk of audit firm failure.		
Comments:		

	Y	**N**
Are you of the opinion that the following information should be included in the transparency report of an audit firm with regards to the governance structure?		
How the audit firm's governance structure and management operate their duties?		
What type of decisions are made by the audit firm's governance structure and management?		
The names and job titles of all members of the firm's governance structures and management?		
How the members of the governance structure and its management were elected or appointed?		
The terms of the members of the governance structure and its management?		
The length of service of the members of the governance structure and its management?		

The yearly meeting attendance of the members of the governance structure and its management?		
Any biographical details of the members of the governance structure and its management?		
Any additional practices and principles from the King IV Corporate Governance Code which it has adopted?		
Comments:		

	Y	N
With reference to the <u>INED directors</u>, are you of the opinion that the <u>transparency report should include</u>:		
Information on the appointment, retirement and resignation of INED directors?		
Information on the remuneration of the INED directors?		
Information on the duties of the INED directors?		
Arrangements by which the INED directors discharge their duties?		
How the firm supports the INED directors in discharging their duties?		
How the firm has positioned its INED directors (on the board or the oversight board)?		
The criteria for assessing the impact of INED directors on the firm's independence as auditors and their independence from the firm and its owners?		
Comments:		

	Y	N
With reference to having a <u>stakeholder-inclusive approach</u>, are you of the opinion that the oversight board of your audit firm should:		
Have a dialogue with listed company shareholders about corporate governance matters?		
Enhance mutual communication and understanding to ensure that the audit firm keeps in touch with shareholder opinion, issues and concerns?		

Disclose on its website its policies and procedures for dialogue with listed company shareholders and listed companies?		
Report on the dialogue the audit firm had during the year?		
Disclose the nature and extent of the involvement of the INED directors in this dialogue?		
Have dialogue with shareholders to enhance mutual communication and understanding?		
Have dialogue with listed companies on the process of recommending the appointment and re-appointment of auditors and make considered use of votes in relation to such recommendations?		
Comments:		

	Y	N
Are you of the opinion that an 'apply and explain' basis will be the most appropriate for an Audit Firm Governance Framework for South African auditing firms? **Please explain your response below.**		

In your opinion, what would be the difficulties in implementing an Audit Firm Governance Framework in South Africa?

	Y	N
Do you believe that auditing firms need to appoint an oversight board which is responsible for the corporate governance of the audit firm, in order to properly fulfil their public interest responsibilities? **Please explain your response below.**		

	Y	N
Do you believe that the audit part of auditing firms needs a specific governance focus that may be different from the governance of the non-audit part of the firm? **Please explain your response below.**		

What are the areas you believe the governance forum of an audit firm should focus on to ensure that the firm is governed in the public interest?

	Y	N
Would you like to receive a copy of the completed research study?		

Please feel free to provide any information below which you might feel is relevant to this study and which has not been addressed in the questionnaire.

Thank you for your time.

Please remember to click on 'submit'.

ANNEXURE O: Email send to the participants by the researcher

Dear XXX

This questionnaire forms part of a PhD study entitled '*The Application of Corporate Governance in Large and Medium Sized South African Auditing Firms'* at the University of Johannesburg under the supervision of Professor Ben Marx. Please see attached the cover letter from Professor Ben Marx.

Approval for the research has been granted by the University of Johannesburg's Ethics Committee and SAAPTI. Please see attached the ethical clearance and the cover letter from SAAPTI.

The questionnaire should be completed electronically.

i. Click on the link below and follow the prompts to complete the questionnaire;
ii. Once you have completed the questionnaire, please click on 'submit';
iii. This questionnaire will take you no more than 20 minutes to complete;
iv. CONFIDENTIALITY: The name of the auditing firm and yourself will not be made public in the research. All information will be treated as strictly confidential and only reported in aggregate;
v. https://forms.gle/UHuuC9XJVW74dzQi9.

VALUE OF YOUR RESPONSE

As your auditing firm is one of the top nine auditing firms in South Africa, your audit firm was selected as part of the population for this study. As a business leader and CEO of an auditing firm, your input is essential. Your input as a leader in corporate South Africa is critical and will be of immense value to the success of the study.

Should you have any objection to completing the questionnaire, please state your reason and return the questionnaire for control purposes.

Thank you in advance

Kind regards, Rozanne Smith.